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IN THE

Supreme Court of the United States

OCTOBER TERM, 1941

No. 265.

FEDERAL POWER COMMISSION AND ILLINOIS COMMERCE COMMISSION, *Petitioners*,

v.

NATURAL GAS PIPELINE COMPANY OF AMERICA AND TEXOMA NATURAL GAS COMPANY, *Respondents*.

No. 268.

NATURAL GAS PIPELINE COMPANY OF AMERICA AND TEXOMA NATURAL GAS COMPANY, *Petitioners*,

v.

FEDERAL POWER COMMISSION AND ILLINOIS COMMERCE COMMISSION, *Respondents*.

Motion of the National Association of Railroad and Utilities Commissioners that Said Association Be Granted Leave to File a Brief Amicus Curiae in Support of the Appeal of the Federal Power Commission Herein, and in Opposition to the Appeal of the Cross Petitioners.

BRIEF OF THE NATIONAL ASSOCIATION OF RAILROAD AND UTILITIES COMMISSIONERS.

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Washington, D. C.

January 12, 1942.

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Motion of the National Association of Railroad and Utilities Commissioners that Said Association Be Granted Leave to File a Brief Amicus Curiae in Support of the Appeal of the Federal Power Commission Herein, and in Opposition to the Appeal of the Cross Petitioners.

I. The National Association of Railroad and Utilities Commissioners is a voluntary Association embracing within its membership the members of the regulatory commissions and boards of the several States of the United States, except Delaware, which has no state regulatory commission, and New York, the commissions of which are not at present actively identified with the Association.

The Constitution of said Association, among others, states as objects of said Association "the promotion of cooperation of the commissions of the several States with each other, and with Federal regulatory agencies" and the "protection of common interests of the people of said States." Said Constitution empowers the President of the Association to direct the General Solicitor to appear on behalf of the Association in any proceeding in any court wherein the President shall consider that the Association should be represented, in furtherance of the objects of the Association.

This motion, and the brief presented herewith, are offered on behalf of said Association by direction of the President of the Association, with the purpose of contributing towards the protection of the interests of the people of the several States of the United States.

II. Said Association further represents that the Natural Gas Act, the constitutionality of which is being contested in the above entitled proceedings, was enacted by Congress upon consideration of a resolution adopted by said Association, on behalf of the State commissions represented in its membership, at its annual convention in 1937, asking Congress to enact such legislation, and upon the consideration of representations made to the Congress by various State commissions, setting forth the necessity for such enactment; and that said brief, if permitted to be filed, will be in support of the proposition that said Act is constitutional, and in support of other propositions of law, the recognition of which by this court, in the above entitled proceedings, is of importance to the people of the several States, and to the said State commissions, as agencies of government, charged with the regulation of the rates of public utilities in said States.

III. On December 12, 1941, counsel for said Association addressed to counsel for the Natural Gas Pipeline Company and Texoma Natural Gas Company, a letter, the body of which was as follows:

"Dear Sir:

"I have been directed by the President of this Association to prepare and offer for filing in the U. S. Supreme Court an *amicus curiae* brief in the Natural Gas Pipeline Company cases, Nos. 265 and 268, in support of the appeal of the Federal Power Commission.

"If you will assent, on behalf of the Natural Gas Pipeline Company, to the filing of such brief, I shall appreciate your courtesy if you will write me a letter expressing such assent, which I may exhibit to the Clerk of the U. S. Supreme Court, when I tender our brief for filing.

"Our brief has not yet been prepared, but I shall seasonably serve copies of the same upon Counsel for the parties.

"This Association represents in its membership the railroad and public utilities commissions of the several States, and will offer the brief on behalf of such commissions in their public capacity.

"In this connection I will say to you that the U. S. Supreme Court has heretofore never denied assent to our filing of a brief, upon a motion for such assent, even when parties have withheld their consent to a proposed filing. I desire, however, if possible to avoid having occasion to make any motion by advising the Clerk of the assent of all parties to the case."

To said letter, under date of December 15, 1941, a response was received, the body of which was as follows:

"Dear Sir:

"This will acknowledge receipt of your letter of December 12 requesting our assent on behalf of Natural Gas Pipeline Company of America to the filing by you of an *amicus curiae* brief in Cases Nos. 265 and 268, now pending before the United States Supreme Court.

"Writs of *certiorari* in said cases were granted on October 13 and you have had more than two months within which to prepare and serve on us a brief, if you had desired to do so. We have not been served with the Solicitor General's brief but only today received a page proof of his proposed brief which he says will be revised before it is finally printed. It will take all of the time available between now and the oral argument to file our reply to the Solicitor General's brief

and prepare for the oral argument. The Solicitor General's brief is very exhaustive and adequately presents all the issues from his viewpoint.

"We have been advised by the Clerk of the Supreme Court that the argument in these cases will be heard during the week of January 12 and it seems to us that if such a brief, which is as yet unwritten, is filed by you, we will not have an opportunity to reply thereto.

"We, therefore, feel that we can not in justice to our clients consent to the filing of an *amicus curiae* brief by you.

"We are forwarding to the Clerk of the Supreme Court a copy of your letter to us, together with a copy of this letter, for his information."

IV. Because the regulatory commissions and boards represented in the membership of said National Association of Railroad and Utilities Commissioners are governmental bodies of the several States of the United States, exercising rate-making powers under the laws of said States, and engaged in the regulation of the rates and services of gas utilities, which, in many instances, purchase their supplies of natural gas at wholesale in interstate commerce from natural gas companies subject to regulation under the Natural Gas Act, and because the brief sought to be filed in their behalf, and tendered herewith, is offered in the public interest of the people of said States, said Association respectfully represents that the filing of such brief, in the above entitled proceedings, ought not to be prevented by the refusal of the aforesaid companies to assent to such filing.

V. Said Association presents herewith a copy of the brief which it desires to file, and respectfully moves that it be granted leave to file the same.

In support of this motion, said Association cites as precedents the action of this court upon similar motions made in the following cases: *Board of Railroad Commissioners* v. *The Great Northern Railway*, 281 U. S. 412; *Public Service Commission of Wisconsin* v. *Wisconsin Telephone Company*, 309 U. S. 657.

In each of said cases the defendant corporation refused to assent to the filing of an *amicus curiae* brief, but in each case, upon motion, and notwithstanding opposition, the court granted leave for the filing of such brief, by reason of the public character of the State commissions and boards, on behalf of which the brief was offered.

Respectfully submitted on behalf of said Association,

JOHN E. BENTON,
General Solicitor of said Association,
7411-15 New Post Office Bldg.,
Washington, D. C.

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OPINION BELOW.

The Opinion of the Circuit Court of Appeals is reported in 120 Fed. (2d) 625. It appears in the Record at Pages 4026-4041. The opinion of the Federal Power Commission appears in the Record at Pages 3925-3942.

STATEMENT OF THE CASE.

For the purposes of this brief we adopt and refer to the Statement of Facts contained in the brief heretofore filed for the Federal Power Commission and the Illinois Commerce Commission.

QUESTIONS ARGUED HEREIN.

This Brief is filed in support of the following propositions:

1. The Court below did not err in not sustaining the contention of the cross-petitioners in the above entitled proceedings, hereinafter referred to as the gas companies, that the order of the Federal Power Commission, hereinafter referred to as the Commission, should be set aside upon the ground that the Natural Gas Act, as applied by the Commission, is in conflict with the 5th Amendment to the Constitution of the United States.

2. The Court below did not err in not sustaining the contention of the gas companies that the order of the Commission should be set aside upon the ground that the Commission is without jurisdiction to enter an "interim order".

3. The Court below erred in holding that the order of the Commission should be set aside upon the ground that the rate base found and determined by the Commission was inadequate in the amount of $8,500,000, claimed by the gas companies as a separate allowance for going value.

4. The Court below erred in holding that the Commission's order should be set aside by reason of the fact that the Commission computed its allowance for amortization, including depreciation of capital assets, upon the basis of the entire service life of such capital assets, instead of upon that part of such service life which remained after the effective date of the Commission's order.

5. The gas companies should refund to their customers the overcharges made since the effective date of the Commission's order.

SUMMARY OF ARGUMENT.

The Natural Gas Act is Constitutional as a Regulation of Interstate Commerce Within the Power of Congress Under the Commerce Clause.

The power of Congress to regulate interstate commerce is plenary, and does not depend upon the public utility character of the enterprises regulated.

The necessity for the regulation provided by the Natural Gas Act was for the decision of Congress.

The gas companies, parties herein, are public utilities.

The Commission Had Jurisdiction to Enter the Order Here Under Review.

The Natural Gas Act was enacted as an aid to State commissions.

Congress intended the Commission to act with expedition.

The demands of due process were fully met.

The Court Below erred in holding that the Rate Base Determined by the Commission was inadequate by reason of the Commission's Treatment of the Gas Companies' Claim Respecting Going Value.

The claim that going concern must be valued separately from other elements of value rests upon a misconception of the so-called Smyth v. Ames rule.

The Commission did not exclude the going concern element in determining the rate base used.

The rate base found by the Commission was designed to represent an appraisal of the entire utility property, including all elements tangible and intangible.

The gas companies are attempting to secure the inclusion in their rate base of an allowance on account of an element which represents no investment by them.

The hazards of the business and other special circumstances held by the court below to require inclusion, in the rate base, of the going value item claimed were properly to be considered only as bearing upon the fair rate of return.

The Court Below Erred in Holding that the Commission's Order Should Be Set Aside Because the Commission Computed the Annual Allowance for Amortization of Capital Assets on the Basis of the Entire Service Life of such Assets.

The Commission properly based its amortization allowance upon the entire service life of the property to be amortized.

The Commission properly based its amortization allowance upon the cost of the property to be amortized.

If the Commission's order was made after a due process of law hearing, the only question open for the consideration of the Court is whether the rates prescribed are clearly shown to be confiscatory.

The ruling in Cotting v. Godard, even if admitted to be sound for application in any case, could not be applied in the administration of the Natural Gas Act without defeating the purposes of the Act.

The Gas Companies Should Refund to Their Customers the Overcharge le Since the Effective Date of the Commission's Order.

Conclusion.

ARGUMENT.

The Natural Gas Act is Constitutional, as a Regulation of Interstate Commerce Within the Power of Congress Under the Commerce Clause.

The power of Congress to regulate interstate commerce is plenary, and does not depend upon the public utility character of the enterprise regulated.

The gas companies before the Commission, and before the Court below, contended that the Natural Gas Act is unconstitutional as violative of the Fifth Amendment of the Constitution, because it undertakes to regulate the prices to be charged by natural gas companies, which they claim to be private enterprises, not subject to regulation as public utilities. This contention was denied by the Commission and by the Court below, and is renewed here.

Upon this point the position of the gas companies is stated at Pages 234-236 of their Brief in this Court as follows:

> "This case squarely presents the question of whether Congress may, under the Fifth Amendment, fix prices on private sales of an ordinary commodity. * * *
>
> "Cross-petitioners' business is of a strictly private character. Cross-petitioners have never held themselves out to the public as common carriers; nor have cross-petitioners offered to sell their gas to the general public * * *. Cross-petitioners have at all times sold their gas by private contracts. * * * Cross-petitioners do not operate under any franchise; they have no monopoly. * * * They are a private purveyor of a commodity."

The power of Congress under the Commerce Clause to regulate prices in interstate commerce is not limited to public utilities. The idea, once widely held, that prices may be regulated only when the owners of property have voluntarily dedicated it to public use, in an enterprise which may be designated a public utility, no longer obtains.

Under the Fifth Amendment the authority of the Federal government over interstate commerce does not differ in ex-

tent or character from that retained by the States over intrastate commerce. *United States* v. *Rock Royal Cooperative*, 307 U. S. 533, 569. We may therefore turn to cases where the effect of the 14th Amendment, upon the power of a State to regulate prices has been considered.

In *Nebbia* v. *New York*, 291 U. S. 502, involving the validity of a State statute regulating the price of milk, it was contended that the 14th Amendment inhibited the regulation. Contentions as to the private character of the milk business were made identical, in the grounds presented, with those presented by the gas companies in this case. In denying the contention thus made, this court said:

> "We may as well say at once that the dairy industry is not, in the accepted sense of the phrase, a public utility. We think the appellant is also right in asserting that there is in this case no suggestion of any monopoly or monopolistic practice. It goes without saying that those engaged in the business are in no way dependent upon public grants or franchises for the privilege of conducting their activities. But if, as must be conceded, the industry is subject to regulation in the public interest, what constitutional principle bars the state from correcting existing maladjustments by legislation touching prices? We think there is no such principle.
>
> The due process clause makes no mention of sales or of prices any more than it speaks of business or contracts or buildings or other incidents of property. The thought seems nevertheless to have persisted that there is something peculiarly sacrosanct about the price one may charge for what he makes or sells, and that, however able to regulate other elements of manufacture or trade, with incidental effect upon price, the state is incapable of directly controlling the price itself. This view was negatived many years ago. *Munn* v. *Illinois*, 94 U. S. 113, 24 L. ed. 77. * * * Munn and Scott held no franchise from the state. They owned the property upon which their elevator was situated and conducted their business as private citizens. No doubt they felt at liberty to deal with whom they pleased and on such terms as they might deem just to themselves. * * * It is true that the court cited a statement from Lord Hale's *De Portibus Maris*, to the effect that when pri-

vate property is 'affected with a public interest, it ceases to be *juris privati* only;' but the court proceeded at once to define what it understood by the expression saying: 'Property does become clothed with a public interest when used in a manner to make it of public consequence, and affect the community at large.' (p. 126.) Thus understood, 'affected with a public interest' is the equivalent of 'subject to the exercise of the police power;' and it is plain that nothing more was intended by the expression. * * * The statement that one has dedicated his property to a public use is, therefore, merely another way of saying that if one embarks in a business which public interest demands shall be regulated, he must know regulation will ensue. * * *

"Plainly the activities of railroads, their charges and practices, so nearly touch the vital economic interests of society that the police power may be invoked to regulate their charges, and no additional formula of affection or clothing with a public interest is needed to justify the regulation. And this is evidently true of all business units supplying transportation, light, heat power and water to communities, irrespective of how they obtain their powers. * * *

"It is clear that there is no closed class or category of businesses affected with a public interest, and the function of courts in the application of the Fifth and Fourteenth Amendments is to determine in *each* case whether circumstances vindicate the challenged regulation as a reasonable exertion of governmental authority or condemn it as arbitrary or discriminatory. * * * The phrase 'affected with a public interest' can, in the nature of things, mean no more than that an industry, for adequate reason, is subject to control for the public good."

In later cases involving the exercise by Congress of its power under the Commerce Clause the court cited and followed the *Nebbia case*, among which were: *United States* v. *Rock Royal Cooperative*, 307 U. S. 533, 568. *Sunshine Anthracite Coal Co.* v. *Adkins*, 310 U. S. 381, 397.

The gas companies base their contention upon the claimed authority of *Tyson Bros.* v. *Banton*, 273 U. S. 418, and upon other cases following that case, or like it in principle. We

believe that the majority opinion in *Tyson Bros.* v. *Banton* was never accepted by lawyers generally, as settling the limits of legislative power under the Fifth and Fourteenth Amendments. At the time of its decision four of the nine Justices of this Court dissented. We believe that the majority opinion in that case, and in other cases like it, will not be accepted as guiding by the court. What was said by the present Chief Justice, in his dissenting opinion in that case, respecting the character of businesses the prices of which may be regulated, may be said to have pointed the way to the decision of this Court in the *Nebbia case.* We quote briefly:

> "The phrase 'business affected with a public interest' seems to me to be too vague and illusory to carry us very far on the way to a solution. * * * The very fact that it has been applied to businesses unknown to Lord Hale, who gave sanction to its use, should caution us against the assumption that the cateory has now become complete or fixed and that there may not be brought into it new classes of business or transactions not hitherto included, in consequences of newly devised methods of extortionate price exaction. * * *
>
> "Statutory regulation of price is commonly directed toward the prevention of exorbitant demands of buyers or sellers. An examination of the decisions of this court in which price regulation has been upheld will disclose that the element common to all is the existence of a situation or a combination of circumstances materially restricting the regulative force of competition, so that buyers or sellers are placed at such a disadvantage in the bargaining struggle that serious economic consequences result to a very large number of members of the community. Whether this situation arises from the monopoly conferred upon the public service companies or from the circumstance that the strategical position of a group is such as to enable it to impose its will in matters of price upon those who sell, buy, or consume, * * * the result is the same. Self-interest is not permitted to invoke constitutional protection at the expense of the public interest and reasonable regulation of price is upheld." (273 U. S. 451-452)

The necessity for the regulation provided by the Natural Gas Act was for the decision of Congress.

Recognizing, as they must, that the decisions above referred to, and others, establish that Congress, under the Commerce Clause, may regulate prices where the circumstances make such regulation reasonable, for the protection of the public interest, counsel for the gas companies argue at much length that the "circumstances" shown in the record render the regulation "arbitrary and discriminatory."

The facts emphasized and relied upon by the gas companies are the very facts which led to the enactment of this legislation by the Congress.

The gas companies, parties to this case, and other pipeline companies, take natural gas from the ground in producing states, and transport the same into other states, where it is, in most instances, sold to distributing companies, which are admittedly public utilities, buying for resale to the public.

Until the Natural Gas Act was enacted contracts of sale by the pipeline companies to the distributing companies were claimed to be private contracts in interstate commerce, beyond the reach of state regulatory authority. It therefore resulted that the rate regulatory authorities of the states, when called upon to establish just and reasonable rates for gas service, found themselves unable to reach and regulate the major part of that service.

The gas service rendered to the public, regulation of which was desired in the public interest, in each particular case was, in fact, a joint service, participated in by the pipeline company and the distributing company. The power of the state regulatory agency, however, extended only to the regulation of the distributing company; and the prices of that company were necessarily, in principal part, controlled by the price exacted by the pipeline company for the gas delivered at the city gate.

The Natural Gas Act, as is stated on Page 226 of the brief of counsel for the gas companies, originated as H. R. 11662

in the 64th Congress. It was reintroduced in slightly amended form as H. R. 4008 in the 65th Congress. The published hearing before the House Interstate and Foreign Commerce Committee shows that the Committee had before it very much information dealing with the difficulties confronting state commissions by reason of the fact that only distributing companies were subject to their regulation.

The President of the National Association of Railroad and Utilities Commissioners appeared and testified before the Committee, in support of the legislation. Other state commission representatives likewise appeared in support of the legislation. A resolution, adopted by the Association at its 1935 annual convention, urging Congress to enact legislation, was presented. The decisions of the United States Supreme Court which established the inability of state commissions to regulate the rates for gas sold at wholesale in interstate commerce for resale were presented to the Committee, and their effects were discussed. Communications from various state commissions were before the Committee giving concrete instances in which the attempts of state commissions to establish reasonable rates for gas service were impeded and rendered impossible of accomplishment by reason of the fact that the interstate pipeline companies were beyond the reach of state regulatory power.

In addition to all this information the Committee had before it the results of the Federal Trade Commission investigation, and other reports made pursuant to the authority of Congress referred to in Section 1 of the Natural Gas Act.

To determine whether the circumstances so shown rendered regulation of the prices for gas sold by such pipeline companies necessary and reasonable was for Congress, as this court pointed out in *Sunshine Anthracite Coal Co. v. Adkins*, 310 U. S. 381. In that case, referring to a somewhat similar contention, in an opinion by Mr. Justice Douglas, the court said:

> "But appellant claims that this Act is not an appropriate exercise of the congressional power. It urges

that the nature and use of bituminous coal in no ways endanger the health and morals of the populace; that no question of conservation is involved; that the ills of the industry are attributable to overproduction. • • • Those matters, however, relate to questions of policy, to the wisdom of the legislation, and to the appropriateness of the remedy chosen—matters which are not our concern. If we endeavored to appraise them we would be trespassing on the legislative domain." (310 U. S. 381, 394, 395)

The gas companies, parties herein, are public utilities.

The gas companies argue with much insistence that they are not public utilities. They assert that they have at no time dedicated their property to public use; and that the Natural Gas Act, in subjecting them to regulation, in effect takes private property for a public use, in derogation of the Fifth Amendment.

This argument begs the question. The mere fact that interstate natural gas pipeline enterprises had not been subjected to regulation prior to June 28, 1938, does not establish their character prior to that date as private enterprises. If they were subject to public regulation upon that date they were so subject prior thereto. They cannot claim immunity from regulation merely because they had long enjoyed immunity, *Producers Transportation Co.* v. *Railroad Commission*, 251 U. S. 228; *Midland Realty Co.* v. *Kansas City Power & Light Co.*, 300 U. S. 109.

The gas companies are public utilities by their own choice. They elected to devote their properties to public utility enterprises when they undertook to produce gas, in the gas fields of Texas, and to transport such gas to the cities of the middle west, and there to effect arrangements whereby it should be distributed to the general public.

Gas pipeline companies are public utilities regardless of the character of the legal arrangements which they effect to complete the rendition of gas service in which they engage. Such arrangements may consist of the construction of distributing lines, owned and operated by the pipeline company,

as in the following cases: *Pennsylvania Gas Co.* v. *Public Service Commission*, 252 U. S. 23; *Peoples Gas Co.* v. *Public Service Commission* 270 U. S. 550; *East Ohio Gas Co.* v. *Tax Commission*, 283 U. S. 465. They may consist of arrangements with distributing companies whereunder the gross amounts paid by customers for gas delivered are shared between the distributing company and the pipeline company, as appears to have been the case in *Public Utilities Commission* v. *Landon*, 249 U. S. 236. The arrangements made may be in the nature of outright sales, such as appear to have been made in *Missouri* v. *Kansas Gas Co.*, 265 U. S. 298, and in this case. In every case, whatever of the form of arrangements effected, the pipeline company establishes, or joins in the establishment of, a public utility enterprise, the continued and efficient service of which to the public, at reasonable rates, is obviously of great importance to the public.

When the pipeline company itself sells directly to customers it is plain that it owes to such customers such service at such rates. If it chooses to effect arrangements with others to share in the enterprise, by distributing within the various localities to be served, the customers are entitled to the same efficient service, at reasonable rates; but such service can be supplied at such rates only if the pipeline company performs its share of the joint enterprise in a proper manner.

The duty thus to perform its share of the enterprise rests upon the pipeline company no less where it effects arrangements to share the enterprise with others than where it carries on the entire enterprise itself. In neither case can the owners of the pipeline say that they have not elected to devote their property to an enterprise effected with a public interest, and subject, at the will of the legislature, to regulation. The very nature of the enterprise, in which they embark their property, is that of a public utility.

The mere fact that interstate gas pipeline companies were not subject to regulation when the gas companies, which are parties to this case, acquired or constructed their properties does not affect the situation. They knew, or must be as-

sumed to have known, that Congress under the Commerce Clause would exercise power to regulate their interstate activity whenever such regulation should appear desirable in the public interest.

The Commission had Jurisdiction to Enter the Order Here Under Review.

The gas companies contend that the Commission's order must be set aside because it was entered before the completion of the rate investigation proceeding, in which it was made, and because it specifically provides that the record "shall remain open for such further proceedings as the Commission shall deem necessary and desirable."

The order both in the Commission's opinion, and in the order itself is termed as "interim order". At page 216 of their Brief, counsel for the gas companies state their contention as follows:

> "We submit that Section 5 of the Natural Gas Act requires that the hearing be completed before an order reducing rates can be entered. Under the plain wording of the statute no authority is given the Commission to enter an order fixing rates until after the completion of a full hearing. There is no provision in the statute for the entering of an interim order."

It may be admitted that there is no such term used in the Act as "interim order", and, further, that the Commission must derive its authority from the Act. Unless the Act, properly understood, authorizes the order here under review, the order must be set aside.

Whether that order was within authority granted, however, depends not upon the bare words of Section 5 of the Act, but upon the intent of Congress, as gathered from the language used in said Section 5 and elsewhere in the Act, read in the light of the situation with which Congress undertook to deal. *American Trucking Association* v. *United States*, 310 U. S. 534, 542-43; *United States* v. *San Francisco*,

310 U. S. 16; *Texas and Pacific Railroad Co.* v. *Gulf etc. R. Co.*, 270 U. S. 266, 277-278; *Railroad Commission* v. *Chicago B. & Q. Railway*, 257 U. S. 564, 586.

The Natural Gas Act was enacted as an aid to state commissions.

The situation with which Congress was faced has been referred to hereinbefore. The states, under the law as declared in *Public Utilities Commission* v. *Attleboro Co.*, 273 U. S. 83, and *Missouri* v. *Kansas Gas Co.*, 265 U. S. 298, were unable to regulate gas utility enterprises effectively when the distributing companies received their gas from interstate natural gas companies. The problem was acute, as was evidenced by the resolution of the National Association of Railroad and Utilities Commissioners, hereinbefore referred to, and the statements and communications placed before Congress by various state regulatory agencies.

The resolution in question concluded as follows:

> "*Resolved further*, That Congress be asked to limit the jurisdiction granted strictly to gas transmitted and sold at wholesale for resale, and that such legislation be so drawn as in no way to limit or impair the power of the States to regulate intrastate and local service, and the rates applicable thereto."

Congress was thus asked to complement State regulatory agencies, not to supplant them.

In this situation, the Natural Gas Act was enacted. The Federal Power Commission was vested with regulatory powers carefully restricted to the Federal field. To meet a demonstrated need, which existed by reason of the inadequacy of State power to regulate sales in interstate commerce for resale, the Federal Power Commission was made a Federal regulatory agency, with respect to those sales, for the plain purpose of enabling State commissions effectively to perform their function of assuring to the public reasonable service at reasonable rates.

The powers of the Federal Power Commission, under the Natural Gas Act, were made complete, with respect to those matters which were beyond State control, but, insofar as service and rates were concerned, extended only to the control of those matters,—that is they extended only to service and the rates for service under contracts for the sale in interstate commerce of natural gas for resale.

Section 17 of the Act authorizes the Commission to refer cases to joint boards, composed of nominees of State commissions, and to "confer with any State commission regarding rate structure * * * (and) to hold joint hearings with any State commission in connection with any matter with respect to which the Commission is authorized to act."

Section 5(b) of the Act provides as follows:

> "5(b) The Commission upon its own motion, or upon the request of any State commission, whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commission has no authority to establish a rate governing the transportation or sale of such natural gas."

This provision enables the Commission to determine the cost of production and transportation by gas companies which produce natural gas in one State and sell the same directly to consumers in another State. Such sales, not being for resale, are not subject to regulation under the Natural Gas Act, but are left to State regulation, as local transactions, within the reach of State power, in the absence of Federal regulation.

As counsel for the gas companies, at page 260 of their Brief, contend, and as the Circuit Court of Appeals said in *Mississippi Fuel Corporation* v. *Federal Power Commission*, 121 Fed. (2nd) 159, 164:

> "Protection of the ultimate consumer and not the intermediate utility was the manifest purpose of the Act."

It follows then that Congress intended the Commission to exercise its powers, in proper cases, to reduce the rates of natural gas companies as a part of an entire process of regulation. The two commissions, acting in their respective fields, were to make orders which, operating together, should require the companies contributing to gas utility enterprises to perform their respective shares of the joint service rendered to ultimate consumers at rates which should be just and reasonable to such consumers.

In this respect the Federal Power Commission is differently situated from the Interstate Commerce Commission when that Commission regulates rates for transportation, and from the Federal Communications Commission, when that Commission regulates rates for transmission of communications. Those Commissions by their orders control the charges which the public shall pay, but the Federal Power Commission is unable to assure ultimate consumers of reductions which are ordered for the public benefit, except in conjunction with the State commissions. The Natural Gas Act was enacted as an aid to the State commissions.

Congress intended the commission to act with expedition.

Congress must then have intended that the Federal Power Commission should so exercise its powers as to enable the entire act of regulation (partly to be performed by the Federal commission and partly by the State commission) to be performed within a reasonable time. An act of Congress will be construed to enable the intention of Congress to be accomplished. *United States* v. *Louisiana*, 290 U. S. 70, 75-76.

The need for expeditious action by the Commission, in order that the public might be granted relief from unreasonable rates with reasonable expedition, was pressed upon the House Interstate and Foreign Commerce Committee when it was considering the bill which finally became the Natural Gas Act.

A communication from the Chairman of the Illinois Commerce Commission, which appears at page 56 of the hearing on H. R. 4008, 75th Congress, making reference to a litigation then going on before that Commission and in the Illinois courts, represented that the Illinois Commission found itself handicapped by reason of its inability to control the prices charged for gas by the Natural Gas Pipeline Company of America. It was urged that the Committee amend the pending bill to include provision for temporary rates, to enable the Commission more expeditiously to prescribe rates, which might be reflected in an order of the Illinois Commission. Mr. Booth, Counsel for that Commission, presented a proposed amendment, which is set forth at page 227 of the brief of counsel for the gas companies filed here.

It is true that the Committee did not include that amendment in the Act. That amendment, however, like the New York and Pennsylvania statutes, was drawn to authorize the Commission to prescribe temporary rates after a hearing only with respect to the amount of the original cost of the property of a regulated company, less depreciation. Under the proposal, the Commission, to compensate the company for any undercharge resulting from that course, would have been authorized to make a proper allowance thereafter, when the Commission should be prepared to determine just and reasonable rates. The order before the Court in this case is widely different in character from the order designed to be authorized by that amendment. This is an order issued after a due process of law hearing, and upon a finding that the rates prescribed will be just and reasonable. That was an order to be issued after a limited hearing, and with no finding as to the justice and reasonableness of the rates to be prescribed.

The fact that Congress did not see fit to adopt that rough and ready method of prescribing rates has no significance as tending to show that it did not intend the Commission to exercise its rate-making powers, whenever the demand of

due process should have been met, and justice should appear to require that rate changes be prescribed.

There are other provisions in the Act which show that it was the intent of Congress to shorten the rate-making process by all means consistent with full protection of the rights of regulated utilities.

After including in Section 4 provisions, common in rate regulatory statutes, commanding that all rates be just and reasonable, and forbidding all discriminatory rates, the Congress in Section 5(a) provided:

> "5(a) *Whenever* the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate * * * is unjust, unreasonable, unduly discriminatory, or preferential, *the Commission shall* determine the just and reasonable rate * * * and *shall fix the same by order.* * * *" (Italics supplied)

The following Sections of the Act are especially significant:

> "Sec. 6(a) The Commission may investigate and ascertain the actual legitimate cost of the property of every natural-gas company, the depreciation therein, and, when found necessary for rate-making purposes, other facts which bear on the determination of such cost or depreciation and the fair value of such property.
>
> "(b) Every natural-gas company upon request shall file with the Commission an inventory of all or any part of its property and a statement of the original cost thereof, and shall keep the Commission informed regarding the cost of all additions, betterments, extensions, and new construction."

> "Sec. 15(b) All hearings, investigations, and proceedings under this act shall be governed by rules of practice and procedure to be adopted by the Commission, and in the conduct thereof the technical rules of evidence need not be applied. No informality in any hearing, investigation, or proceeding or in the manner

of taking testimony shall invalidate any order, decision, rule, or regulation issued under the authority of this act."

"Sec. 16. The Commission shall have power to perform any and all acts, and to prescribe, issue, make, amend, and rescind such orders, rules, and regulations as it may find necessary or appropriate to carry out the provisions of this act. * * *"

Section 8(a) empowers the Commission to prescribe accounts to be kept by natural gas companies, showing the results of their operations. Section 10(a) requires every natural gas company to file with the Commission such annual and other periodic or special reports as the Commission by rule or order shall require.

The Commission was thus equipped with powers enabling it to require natural gas companies to supply information which might make the basis for the fixing of a rate base, and for the determination of reasonable rates, without the costly and time-consuming labors, and testimony of experts, which had become common in endeavors to meet the supposed requirements of the so-called *Smyth* v. *Ames* rule. Congress must have expected these powers to be used. We think it is apparent that its intent was that the Commission should base its rate regulation upon the original cost of the properties regulated, using such cost as sufficient evidence of their fair value, required as a rate base. For that reason Congress studiously avoided any reference to reproduction cost.

At the time the Natural Gas Act was framed and reported to the House, however, and when it passed the House, *Railroad Commission* v. *Pacific Gas & Electric Co.*, 302 U. S. 388, hereinafter discussed, had not been decided. There was still uncertainty as to whether a rate regulatory commission was at liberty to base a finding of rate base value upon original cost, without the ascertainment also of the reproduction cost, in conformity with the supposed requirements of the *Smyth* v. *Ames* rule.

The last Congressional hearing upon the legislation was before the House Interstate and Foreign Commerce Committee on March 25, 1937. The bill was reported by that Committee on April 28, 1937, and was passed by the House on July 1, 1937. It was finally passed by the Senate on June 14, 1938.

Upon consideration of the situation, with respect to which Congress was legislating, and of the provisions of the Act to which we have referred, we think it is evident that Congress intended that the Commission should act expeditiously, whenever a State commission should invoke its aid, or whenever a proceeding before it should be otherwise instituted. For that reason it so equipped the Commission with powers that the Commission might require the regulated utilities to supply information upon which it might act without making a physical valuation. However, because of uncertainty as to this attitude of the Courts, the Commission was given authority, in Section 6(a), to find "other facts" bearing on fair value, "when found necessary".

The demands of due process were fully met.

While Congress, by the provisions of the Act to which we have referred, thus sought to procure expeditious Commission action, it undoubtedly intended to require a due process of law hearing, with notice, and with full opportunity to present evidence and make argument. Such opportunity was given in this case.

There was a hearing which extended through several months, with hearing sessions on fifty-six days. Under the procedure adopted by the Commission the gas companies were first heard. They presented thirty-seven witnesses, which were all they desired to present, and they testified fully. Counsel for the gas companies cross-examined all witnesses offered by the other parties, and offered all the rebuttal they desired to offer. They filed briefs, and were heard in oral argument.

Nowhere in the brief filed for the gas companies is it claimed that there was any failure of proper notice, or any refusal to hear all such evidence and arguments as they desired to present. The complaint, instead, is of the procedure followed.

In their brief, at page 216, complaint is made that the gas companies "were required to proceed with their testimony before the Commission and complainants were required to develop any evidence in support of their contention that cross-petitioners' existing rates are unjust and unreasonable". It is complained that they "have never developed such evidence", and that thirty of the witnesses produced by the gas companies were never cross-examined; and also that the order contains a paragraph holding the proceeding open "for such further proceedings as the Commission may deem necessary or desirable."

It is a singular contention that a hearing is rendered unfair because other parties do not testify, and because witnesses are not cross-examined. We do not extend this brief by argument concerning those alleged grounds of invalidity.

There remain only the contentions that the gas companies were required to be heard first, and that the order was made before the conclusion of the entire investigation proceeding.

With respect to the first matter, the provisions of Section 15(b) of the Act, herein before quoted, would appear to be conclusive. Furthermore, it may be observed that the Commission's procedure, which was designed to facilitate the hearing by permitting the gas companies to produce evidence which might form the basis of a judgment as to the reasonableness of their rates, was entirely in harmony with the plain purposes of the several provisions of the statute, above referred to, which would have permitted the Commission to call upon the company for special reports designed to serve the same purpose.

As to the entry of the order without awaiting completion of the proceeding, no extended argument should be neces-

sary, in view of the scope and purpose of the Act, and of the several provisions to which we have pointed, as manifesting the intent of Congress that the Commission should be able to act with expedition.

When the Commission knew facts which indicated that the charges of the gas companies were probably too high, it was its duty to act with expedition. Especially was this true when a State commission was before the Commission representing that it had been for three years engaged in hearings and in litigation endeavoring to establish just and reasonable rates to the people of the great city of Chicago, upon the gas brought into Illinois by these gas companies, and that a decision and order by the Commission was essential for that purpose. (R. 25-31).

We have pointed out that the Natural Gas Act was enacted to enable the Federal Power Commission to complement State commissions. It was the duty of that Commission so to construe and apply the Act as to coordinate its action with the action of the Illinois Commerce Commission, just as it is the duty of a court, in the construction of a regulatory statute, to construe the same so that administrative and judicial action may be coordinated to accomplish the purpose of the legislation. *United States* v. *Morgan*, 307 U. S., 182, 190-191.

Knowing that the rates of the gas companies ought to be reduced, it was the Commission's duty to reduce them as expeditiously as possible. As the court below has pointed out, it might have concluded the hearing, and thereupon have made a final order. Later it could have instituted another proceeding for the completion of its rate investigation. The law is not so silly as to require that to be done.

The Court Below Erred in Holding that the Rate Base Determined by the Commission Was Inadequate by Reason of the Commission's Treatment of the Gas Companies' Claim Respecting Going Value.

The gas companies claimed a rate base including the following items:

Reproduction Cost, $56,302,250.
Value of Gas Reserve, $13,334,775.
Going Concern Value, $8,500,000.
Working Capital, $975,000.
Prospective additions prior to December 1, 1942, $3,308,399.

The last mentioned item was their estimate of such prospective additions, and was made as a part of a claim of $6,046,286, which they claimed to represent the average investment for future capital additions from the date of their reproduction cost estimate to December 31, 1954, the estimated end of the useful life of the companies gas properties. The witnesses admitted depreciation, termed by them "viewed depreciation," estimated at $2,866,758.

The Commission rejected the $8,500,000 item. The total of the other items, however, without deduction for depreciation, amounting to $74,420,424, was adopted as a rate base.

The gas companies contend that the Commission thereby denied them any allowance for the going concern element of value, and that the rate base fixed is consequently inadequate, as a basis for the computation of reasonable rates, The Court below sustained that contention.

We maintain that the ruling of the Court was based upon a misconception both of what the Commission did and of the law as established by the pertinent decisions of this Court.

The claim that going concern must be valued separately from other elements of value rests upon a misconception of the so-called Smyth v. Ames rule.

Under the decisions of this Court, the test as to the constitutional validity of rates, fixed by legislative authority has been the sufficiency of such rates to yield a fair return on a rate base, which the Commission has denominated "fair value."

The fair value tests was first announced in *Smyth* v. *Ames*, 169 U. S. 466, in which case the Court said:

> "We hold, however, that the basis of all calculations as to the reasonableness of rates to be charged by a corporation maintaining a highway under legislative sanction must be the fair value of the property being used by it for the convenience of the public. And, in order to ascertain that value, the original cost of construction, the amount expended in permanent improvements, the amount and market value of its bonds and stock, the present as compared with the original cost of construction, the probable earning capacity of the property under particular rates prescribed by statute, and the sum required to meet operating expenses, are all matters for consideration, and are to be given such weight as may be just and right in each case. We do not say that there may not be other matters to be regarded in estimating the value of the property. What the company is entitled to ask is a fair return upon the value of that which it employs for the public convenience. On the other hand, what the public is entitled to demand is that no more be exacted from it for the use of a public highway than the services rendered by it are reasonably worth." (169 U. S. 466, 546, 547)

The language just quoted is often referred to as the *Smyth* v. *Ames* rule. It is obvious, however, that it is no rule at all, beyond its requirement that "fair value" be found, and used as a basis for determining rates which the owner of the property involved must be permitted to earn to avoid confiscation.

That this "fair value" was not exchange value was evident, both from the classes of evidence which the opinion states were entitled to consideration, and from the concluding statement, set forth in the language just quoted, that "what the public is entitled to demand is that no more be exacted from it for the use of a public highway than the services rendered by it are reasonably worth."

This limitation of rates to a level not exceeding the worth of services covered, coupled with the consideration of both original cost and present cost, either one of which might tend to support a value either more or less than exchange value, was sufficient to make it clear that "fair value," according to the conception of the Court, was something different from exchange value.

Under this so-called *Smyth* v. *Ames* rule, public service companies, with a very substantial degree of success, have endeavored to build up a procedure which would protect them from the exercise of the right of the people, through their legislative agencies, to impose a just and reasonable regulation upon public service enterprises. Because the present cost of producing their properties had been said to be proper for consideration, they have insisted that such cost must be stated, and have insisted, as a constitutional right, upon the opportunity to make appraisals of the multitudinous units of their properties, and to present evidence of such appraisals in hearings consuming months of time.

The courts have acquiesced in these demands, to the extent of holding that such evidence must be received and given due consideration. *Wilcox* v. *Consolidated Gas Co.*, 12 U. S. 19, 41. *Southwestern Bell Tel. Co.* v. *Public Service Commission*, 262 U. S. 276, 287. The courts also have held that the fair value should be fixed as of the time the rates were to be effective. *San Diego Land, Etc. Co.* v. *National City*, 174 U. S. 739, 757. *Wilcox* v. *Consolidated Gas Co.*, 212 U. S. 19, 52. *Minnesota Rate Cases*, 230 U. S. 352, 434.

This rule requiring the value to be fixed as of the time of the use of the property, under the rates to be fixed, being

established, public service companies not only claimed the right to make and present their reproduction cost estimates, but they claimed that the reproduction cost of the property included the cost of reproducing the business which they were doing, and that such reproduction cost represented the present value of their property, upon which they had a constitutional right to earn a fair return.

To an extent they were successful in imposing this claim upon Commissions and courts. The use of reproduction cost estimates became common, and was treated as proper by this court. *Denver* v. *Denver Union Water Co.*, 246 U. S. 178, 191. In *Southwestern Bell Tel. Co.* v. *Public Service Commission*, 262 U. S. 276, the court went so far as to set aside the Commission rate order involved in that case, because it appeared from the Commission's report that it had not based its findings of fair value upon reproduction cost prices as of the date of the valuation. See also *McCardle* v. *Indianapolis Water Co.*, 272 U. S. 400, 410.

The cost and delays incident to recurring reproduction cost estimates were so great that attempts were made to obviate the necessity for them by the development of cost indices showing the trend of reproduction cost prices, which could be used to indicate the change in the reproduction cost of property from one date to another. The difficulties inherent in the attempts, or in the manner in which they were used, led to the rejection of their results in court. *West* v. *Tel. Co.*, 295 U. S. 662, 667. *Ohio Bell Tel. Co.* v. *Public Utilities Commission*, 301 U. S. 292, 296.

The results of attempting to follow this *Smyth* v. *Ames* rule, as it had been thus developed, are well known. They were commented upon in the dissenting opinions of Mr. Justice Brandeis in *St. Joseph Stockyards Co.* v. *United States*, 298 U. S. 73, 84, and, of Mr. Justice Black in *McCart* v. *Indianapolis Water Co.*, 302 U. S. 419, 435.

Some Commissions refused to undertake to make physical valuations under the *Smyth* v. *Ames* rule, and frankly followed the practice of treating the investments of companies as a sufficient basis for determination of their rate

bases. Notable among these was the Railroad Commission of California.

This practice of the California Commission came squarely before this court in a case determined in January, 1938. An epic-making decisions resulted. The case was *Railroad Commission* v. *Pacific Gas and Electric Co.*, 302 U. S. 388.

The United States District Court of Northern California had enjoined the enforcement of a rate reduction order of the California Commission upon the ground that the Commission had failed to find the value of the property of that company in accordance with the *Smyth* v. *Ames* rule. It appeared that the Commission had received evidence presented by the utility as to the reproduction cost of its property, but had refused to make use of the same in determining the rate base, stating in its report that it found the same unsatisfactory. As a rate base the Commission used the historical cost of the property involved, without making any finding of value either for the going concern element or for the property as a whole. Upon an appeal to this court, from the action of the District Court, this court said:

> "The Commission was entitled to weigh the evidence introduced, whether relating to reproduction cost or to other matters. The Commission was entitled to determine the probative force of respondent's estimates. That the Commission did so is apparent from both its statement to that effect and the reasons it gives for considering these estimates to be without positive value. * * * Nor did the ruling with respect to the weight of evidence as to reproduction cost leave the Commission without evidence of the value of respondent's property. We have frequently held that historical cost is admissible evidence of value. * * * In the instant case we cannot say that the Commission in taking historical cost as the rate base was making a finding without evidence and therefore arbitrary. * * * The Commission specifically found what it considered to be the rate base. 39 Cal. R. C. supra, p. 76. The Commission found that rate base to be reasonable. Id. p. 77, note. The import of its opinion is that the rate

base represented the Commission's conclusion as to the value which should be placed upon respondent's property for the purpose of fixing rates." (302 U. S. 388, 397, 398, 399, 400)

The case was remanded to the District Court for findings on the question of confiscation, which this court held to be the only question open.

From this opinion Mr. Justice Butler, who had written the opinion of the court in the *McCardle case*, wrote a long and vigorous dissent, which was joined in by Mr. Justice McReynolds, who had written the opinion in the *Southwestern Bell Telephone Company* case. The following may be quoted from that dissent:

> "The principle applied in Smyth v. Ames has long governed wherever judicial action has been invoked to enforce the rule of just compensation. It is binding upon state courts and commissions. But the California commission refuses to follow the established rule. It does not ascertain or use present value but in its place takes historical cost, actual or estimated, as the basis of its determination in rate judging and rate making. * * * I cannot refrain from protesting against the Court's refusal to deal with the case disclosed by the record and reasonably to adhere to principles that have been settled. Our decisions ought to be sufficiently definite and permanent to enable counsel usefully to advise clients. Generally speaking, at least, our decisions of yesterday ought to be the law of today."

This dissent indicates not only the misconstruction which the dissenting Justices had placed upon the opinion in *Smyth* v. *Ames*, but it indicates also that they realized that the doctrine of the opinions, applying the *Smyth* v. *Ames* rule, which they discussed in their dissent, was being discarded. The full significance of the opinion will be commented upon a little later in this brief.

The commission did not exclude the going concern element in determining the rate base used.

We return now to the claim of the gas companies that they have been denied all recognition of the going value element, which is claimed to inhere in their property.

This claim rests upon the fact that the Commission refused to include in the rate base the item of $8,500,000, which experts for the gas companies had testified should be included for that element, and, upon the further facts that the witnesses who presented reproduction estimates had testified that such elements had included nothing for going value, and that the Commission, in its opinion, stated that it "accepted" the evidence as to reproduction cost.

This statement of the Commission, and the Commission's further statement that the $8,500,000 claim must be disallowed appear to have misled the Court below.

The rate base found by the commission was designed to represent an appraisal of the entire utility property including all elements tangible and intangible.

In fixing the rate base at $74,420,424, the Commission was not making a valuation of the several elements of value, concerning which the witnesses had testified. It was, instead, fixing an amount which would, in the judgment of the Commission, based upon a consideration of all the evidence before it, represent the maximum amount upon which the companies were justly entitled to a fair return.

As originally expressed, the so-called *Smyth* v. *Ames* rule had not exalted reproduction cost evidence above every other class of evidence mentioned, nor held that reproduction cost represented minimum fair value, to which additions must be made for other elements of value, if existing. Care had been taken by the Court in *Smyth* v. *Ames* to make it clear that the enumeration of elements to be considered was not designed to be exclusive, and that the weight to be attributed to each class should be what the valuing tribunal deemed "just and right in each case." The Court was not

laying down a rule to deprive legislators and legislative rate making-agencies of the exercise of their judgment.

Later in *Minnesota Rate Cases*, 230 U. S. 352, Mr. Justice Hughes said:

> "The ascertainment of that value is not controlled by artificial rules. It is not a matter of formulas, but there must be a reasonable judgment having its basis in a proper consideration of all relevant facts." (230 U. S. 434)

When Mr. Justice Hughes had become the Chief Justice, and came to write the opinion in the *Pacific Gas and Electric Company* case, from which we have quoted, he but expressed again what he had said more than twenty years before.

The opinion in the *Pacific Gas and Electric Company* case cleared away excrescencies from the rule as originally expressed by Mr. Justice Harlan.

Under the law, as recognized and emphasized in the later opinion, a rate-making agency may weigh the relevant evidence before it, and, attributing to each piece of evidence the weight it considers just, may determine the amount upon which the owner of the property regulated should be permitted to earn a return; and within the limits of the constitutional rule, which forbids confiscation, its decision is final.

There is no requirement in the constitution, nor in the decision of this court, which compels a regulatory agency to attempt to segregate the intangible elements of a utility's property, such as its established business, from its tangible physical properties, and to determine and state a value for such intangible elements.

It is true that when a commission has followed that method in fixing value, the Court has sometimes expressed approval. The Court has also repeatedly declared the obvious fact that an established plant, in operation and earning money, has greater value than the bare bones of the plant without business; and it has declared that this ele-

ment of value, commonly referred to as going concern value, must be given consideration in fixing value for rate purposes. *Des Moines Gas Company* v. *Des Moines*, 238 U. S. 153, 164; *Denver* v. *Denver Union Water Co.*, 246 U. S. 178, 191; *Los Angeles Gas and Electric Co.* v. *Railroad Commission*, 289 U. S. 287, 314.

The Court, however, has made it clear that going concern value, when existent, inheres in the property because it represents unrecouped investment, made by the owner of the property valued. In the *Des Moines Gas Company case*, just cited, the Court, in sustaining a valuation in which an item for going value had been excluded, said:

> "Included in going value as usually reckoned is the investment necessary to organizing and establishing the business which is not embraced in the value of its actual physical property. In this case, what may be called the inception cost of the enterprise entering into the establishing of a going concern had long since been incurred. The present company and its predecessors had long carried on business in the city of Des Moines, under other ordinances, and at higher rates than the ordinance in question established. For aught that appears in this record, these expenses may have been already compensated in rates charged and collected under former ordinances." (238 U. S. 165-166)

This going concern element must represent investment, as distinguished from losses resulting from lack of income in the early years of the enterprise. *Galveston Electric Co.* v. *Galveston*, 258 U. S. 388; *Houston* v. *Southeastern Bell Tel. Co.*, 259 U. S. 318, 324-325.

By repeated decisions the Court has approved valuations in which the property had been valued as an assembled whole, with no separate appraisal of the going concern element. *Cedar Rapids Gas Co.* v. *Cedar Rapids*, 223 U. S. 655, 669; *Des Moines Gas Co.* v. *Des Moines*, 238 U. S. 153, 164, 165; *Los Angeles Gas and Electric Co.* v. *Railroad Commission*, 289 U. S. 287, 313-317; *St. Joseph Stockyards Co.* v. *United States*, 298 U. S. 38, 62-64; *Driscoll* v. *Edison Light and Power Co.*, 307 U. S. 104, 117.

The Commission, in the case now before this Court, had before it much evidence in addition to the evidence relating to reproduction cost, prospective additions, the $8,500,000 item, and working capital. This other evidence included the original cost of the properties,—shown to be only $60,952,279 (R. 3937),—and the entire financial history of the company, which appears to have been highly profitable. The Commission might well have found that whatever investments were made in the establishment of the business, if any, had been more than recouped by later profits in excess of a fair return.

The Commission considered the property as an assembled whole, and, upon all of the evidence before it, reached the conclusion that an amount equal to the reproduction cost claimed by the companies, plus the amount which they claimed to be the value of their gas reserves, plus the amount which they estimated would be invested for additions and betterments prior to December 31, 1942, plus the full amount of working capital which they claimed to be necessary, would make the maximum amount which could justly be used as a rate base, upon which to compute rates.

That the Commission did not limit its consideration to reproduction cost of plant, value of gas reserves, prospective additions and betterments and working capital is clear from what the Commission said in its opinion, which may be quoted as follows:

> "The companies' claim of $8,500,000 for going concern value must be disallowed. The amount obviously is an arbitrary claim, not supported by substantial evidence warranting its allowance. Its allowance would mean the acceptance of a deceptive fiction, resulting in an unfair imposition upon consumers. We are convinced that we are allowing in our rate base more than an adequate amount to cover all elements of value.
>
> "In disposing of the motion for interim order, we are accepting at this time the companies' estimates of

Reproduction Cost New of Physical Properties (exclusive of Gas Reserves)	$56,302,250
Value of Gas Reserves	13,334,775
Capital additions for the period June 1, 1939 to December 31, 1942	3,808,399
Working capital	975,000
Total Rate Base	$74,420,424

The foregoing amount allowed as a rate base may be compared with book cost of properties, plus working capital of $975,000, as of December 31, 1939, totalling $60,952,279, and therefrom it is clearly disclosed that the rate base presently allowed herein is liberal. This appears especially true when the period of construction is taken into consideration." (R. 3936, 3937)

In determining the import of what the Commission said, it is important to consider the situation with which the Commission was confronted. The gas companies had completed their evidence in chief, concerning their properties and business. Their experts had testified as to their estimates of the reproduction cost of the plant properties. Other witnesses presented by them had testified as to the present market value of the gas reserves used in the business. None of these witnesses had been cross-examined. No rebuttal evidence had been presented.

That the estimates, so made and testified to, were in no respect excessive was scarcely to be expected. Nevertheless, the complaining State commission was before the Commission upon a motion, in which counsel for the Commission joined, asking that those estimates be accepted as entirely accurate, for the purpose of making an immediate decision upon the record, as to the reasonableness of the companies' rates.

Upon consideration of the entire record, it was manifest that, even if the evidence just referred to should be treated as correct, as to the matters to which it related, no rate base could be found which would justify the rates being currently charged.

It was under such circumstances that the Commission said:

> "For the purpose only of disposing of the problem presented by the motion before us, we reluctantly accept the companies' estimate of reproduction cost, their claimed present value of gas reserves, and also their claim for working capital." (R. 3936)

It is not necessary to point out that the evidence thus "accepted" was not evidence as to the amount of the rate base value. It was the Commission's function to fix that value. The witnesses were testifying as to various evidentiary facts. Some testified as to what it would cost to reproduce certain properties,—not as to their value at all. Other witnesses testified as to the present market value of the companies' gas reserves, as gas properties.

For the purpose stated, the Commission accepted the evidence of those witnesses as correctly stating the facts as to which they testified.

The companies' experts had also testified that $8,500,000 ought to be included in the rate base value on account of intangible elements. The nature of this claim, and the manner in which the estimate was made were stated at length in the brief filed for the Federal Power Commission and Illinois Commerce Commission at pages 39-54.

The Commission considered the evidence relating to the $8,500,000 item, and found it not entitled to weight. The estimates which the Commission had accepted as to reproduction cost included not alone the bare material and labor costs but other allowances, which were described by one of the witnesses as follows:

> "The general overheads which we have included in our report consist of engineering and superintendence, organization and law expenditures during construction, preliminary operations, and interest during construction.
>
> "By 'preliminary operations' is meant the expense of tuning up the system and placing it in a position to operate, together with the necessary costs of carrying

such portions of the investment as must be purchased at the start throughout the construction period * * *" (R. 1224)

In *Des Moines Gas Co.* v. *Des Moines*, 238 U. S. 153, 171, the Court specifically held that when allowances for items of the character mentioned had been included the Court could not say that the element of going value had not been given the consideration it deserved.

The Commission also considered the original cost of the property above stated, $60,952,279, and the period of construction, and was convinced that if $74,420,424 should be taken as the rate base, it would be "more than an adequate amount to cover all elements of value"; and that the addition of the $8,500,000 item would result in an "unfair imposition upon the consumers," in the rates thereafter to be fixed by the Illinois Commission.

The decision of the Court in *Railroad Commission* v. *Pacific Gas and Electric Co.*, 302 U. S. 388, hereinbefore referred to, conclusively establishes the propriety of the Commission's procedure in valuing the property as an assembled whole, upon the consideration of the original cost and such other evidence as was before it, disregarding wholly the evidence of the experts as to the $8,500,000 item, which it found not substantially supported.

The gas companies are attempting to secure in their rate base the inclusion of an allowance on account of an element which represents no investment by them.

What the gas companies are attempting to do here is what utilities customarily undertake to do when their properties are valued for rate purposes. They are attempting to secure the inclusion of an item which is fictitious, in the sense that it represents no investment made by the utilities.

They refuse to recognize the wide distinction between fair value for rate purposes and exchange value. Some justification for this may be found in the fact that the Courts have not always appeared to make this distinction. Never-

theless, the decisions of this Court, to which we have referred, establish the distinction.

In the determination of exchange value, the going concern element must, of course, always be given weight. The business attached to any operating property is one of the most important elements in determining what it will earn, and its exchange value. The cases which we have cited, however establish that such going concern element is not properly to be given any weight whatever in determining fair value for rate purposes, unless it is shown to represent unrecouped investment by the utility. It is because allowance for going concern depends upon proof of investment unrecouped that the Court said in *Houston* v. *Southwestern Bell Tel. Co.*, 259 U. S. 318, 325:

> "Whether going-concern value should be considered and allowed at all in determining the base for rate-making, and, if allowed, what the amount of it should be depends upon the financial history of the Company."

Utilities, of course, would gain tremendously if they could induce the Courts to lay down a formula under which a regulatory commission would be compelled to fix the rate base of a utility by first determining the cost of reproducing the physical assets of the utility, conceived of as not possessing any business, but as prudently constructed in the expectation of obtaining business sufficient to utilize such property, in its full extent, and then by adding to such reproduction cost an estimated cost for securing the business which the utility, at the time of the valuation, is shown to be doing.

Inasmuch as the business which a utility is doing at any given time ordinarily represents no investment by the utility, but has been attached in the ordinary course of business, the cost of attachment having been paid out of operating expenses, that method of valuing utility properties would be eminently satisfactory to the utilities. This Court, however, has never laid down that formula.

Notwithstanding the decisions by this Court, to which we have made reference in this brief, utilities, with insistence

and with great ingenuity, persist in the attempt to convince the commissions that every utility in successful operation possesses a going concern element of value, for which an allowance must be made in addition to the full cost of physical properties. The inclusion of such an allowance is claimed as a constitutional right, without proof that it represents any unrecouped investment.

We maintain that the law can not entitle utilities to such an allowance, unless there lies hidden in the Constitution a provision which makes the owners of a public service properties a favored class, entitled, at the expense of the public, to reap where they have not sown, by enjoying a fair return *and something more,* the excess being an increment which accrues, without addition by the owner, through the mere increased need of the public for utility service, and the consequent growth of the business attached.

In this case the gas companies, at pages 87-88 of their brief, make complaint of the regulatory commissions, because of their refusal to allow utility claims for going concern value without proof of investments supporting the same. In concluding their complaint, they say,

> "We submit that the time has come when this issue should be met by the regulatory bodies, and met squarely. If the regulatory bodies are determined to refuse the allowance of going concern value, uniformly upheld by the courts for many years, they should be required to do so candidly, so that the right of review in the courts cannot be circumvented. Let us have an end of this ruse of denying such an allowance and then seeking to cover up the denial under the pretense that all elements of value were considered in arriving at the proper rate base and the amount to be amortized."

We take this to be an adjuration of the Court to do something to clarify the situation. We join with counsel for the gas companies in considering that clarification of the situation is necessary, and join them in asking for it. We do not, however, think that the clarification is necessary for the purpose of bringing the regulatory commissions of the country

to an observance of the constitutional rights of utilities. Their anxiety to observe those rights has been evidenced by their attempts to conform to the supposed requirements of the so-called *Smyth* v. *Ames* rule. Our view is that a clarification is necessary for the purpose of enabling such commissions, with confidence, to apply the rule announced in *Smyth* v. *Ames*, according to its original intent, as reestablished by the opinion in the *Pacific Gas and Electric Co.* case.

We ask the Court to make it clear that a rate regulatory commission may make its determination of the rate base without any attempt to determine the reproduction cost of properties, unless the evidence before the commission is such as to show that justice requires such cost to be estimated and considered in fixing the rate base.

In its opinion in *Smyth* v. *Ames*, this Court, in its enumeration of elements to be considered in determining fair value, mentioned "the amount and market value of its bonds and stock." That element, however, has since been recognized to be of such doubtful aid in determining a just rate base that it is now seldom mentioned by commissions or courts.

While reproduction cost is undoubtedly much better evidence of the amount upon which a utility should justly be permitted to earn a return than the cost and market value of its bonds and stock, it is nevertheless, true that the opportunities which the making of hypothetical reproduction cost estimates afford for the inclusion of items of cost never, in fact, incurred are such that such estimates are often not dependable evidence of fair value.

Furthermore, the delays incident to the preparation and presentation of such estimates are a serious handicap to effective regulation of utility enterprises. In addition, the costs of making physical valuations upon a reproduction cost basis run into great amounts. Such costs, when incurred by utilities, are loaded back upon the public in increased operating expenses; but this is not the worst feature of the situation. The worst feature is found in the fact that regulatory commissions, especially the regulatory commissions of the

smaller states, are not supplied with funds to meet the corps of highly paid so-called valuation experts, who are employed to prepare reproduction cost estimates, and to present the same before commissions and courts. Individual rate payers do not have a sufficient stake in the result of rate proceedings to assume such costs. The result is a one-sided struggle, with a resulting record, finally brought into court, with respect to which the Court may say: "This evidence of reproduction cost, offered by the utility, greatly exceeding the fair value found by the Commission, is practically uncontroverted."

It ought not to lie within the power of a utility to compel a regulatory commission to choose between expending large sums of public money to make reproduction cost estimates (which the commission knows to be not necessary for a just appraisal), or to allow a one-sided record to be made by the utility, at the expense of the rate payers, in which professional, so-called experts will present evidence of valuations which will consume months of time in the presentation, but will, when presented, be of no aid to the commission in reaching its determination.

If it is the judgment of the commission that estimates of reproduction cost will, in fact, be less dependable than original cost, as an aid in the determination of a proper rate base, why should the commission be compelled to consume months or years in either making or receiving such estimates? If, after the record is made, the commission may exercise its judgment to attribute controlling weight to original cost, and to disregard reproduction cost estimates,—as it may under the *Pacific Gas and Electric Co.* opinion—may it not use its judgment *before the estimates are made*, and say to the utility: "Unless facts are presented to us which show that a just determination of the rate base can not be made without a determination of the reproduction cost, we will not make such a determination. It is our present judgment that the evidence of original cost, which can be placed before us, will be a better indication of value for rate pur-

poses than reproduction cost. Therefore, we will not receive reproduction cost estimates."

If the Court will make such a pronouncement, it will protect the rights of all parties. It will save vast amounts of money now being wasted in the preparation and presentation of such estimates, and it will enable the regulatory commissions of the country to perform their rate making function more effectively, because they will be enabled to avoid the expense and the interminable delays which are inevitable, when utilities may demand the right to make and present reproduction cost appraisals.

The right of utilities to judicial protection against confiscation would not be jeopardized by such a pronouncement, since a utility always could come into court upon a claim of confiscation. When the facts are such as to make necessary a determination of the reproduction cost to avoid confiscation, the Court can act, if such determination is denied by the regulatory commission. For example, if we should come into a period of extreme inflation, when a rate base equal in dollars only to the original cost incurred prior to the period of inflation would be manifestly unjust, the commission would adopt means to make the rate base reflect the decreased value of the dollar, or it would permit reproduction cost estimates to be shown. If it failed to do this, the Court, upon review could grant relief.

Such a pronouncement as we are suggesting would restore to the commission the right to exercise judgment, which the court intended to preserve under its opinion in the *Smyth* v. *Ames case.*

The rule laid down in that case,—if it should be termed a rule,—was a judgment rule. It enumerated facts which were proper for consideration, but as we have pointed out before, it declared that the weight to be given to those facts should be determined by the valuing tribunal (subject, of course, to such review by the courts as the Constitution assures). Ever since the decision of the case, however, those representing public service enterprises have sought to procure the exten-

sion of judicial control to such an extent as to rob the regulatory agencies of the opportunity to exercise judgment. Such attempts, at times, have seemed perilously near to success. The judgments of the courts have not been consistent. Nevertheless, the Court has steadfastly refused the promulgation of a valuation formula, and has preserved the judgment principle, although circumscribing it unhappily at times.

In the *Pacific Gas and Electric Co. case* this Court restored the rule. What is now needed is a declaration which shall make clear the full import of that decision, so that a commission may exercise its judgment as to whether the rate base ought justly to be determined upon consideration solely of original cost evidence, or of reproduction cost evidence, or of both; and so that, when it has determined that either class of evidence will not be helpful, it may refuse to receive the same.

As an aid to the understanding of the true intent of the opinion in *Smyth* v. *Ames*, it is useful to consider the situation with which the case dealt.

Rates prescribed by a Nebraska statute were contested by the Receiver for the Union Pacific Railroad. That road was built during and immediately following the Civil War, when prices of both labor and materials were abnormally high. The carrier claimed that the capitalization of the road, which it treated as representing the original investment therein, must be taken as the base, while the State of Nebraska, speaking through William Jennings Bryan, argued in favor of the cost of reproduction.

The court sought to enunciate a rule which would protect the public against unduly high rates (such as it evidently felt might result in some cases from recognizing the original investment as the controlling factor) but which would, nevertheless, assure justice to the investors.

Original cost as a basis, it had been pointed out by Justice Brewer in the lower court, might be unjust to the public because representing funds dishonestly or unwisely spent.

Reproduction cost might be unjust to the carrier because not reflecting honest investment prudently made. And so, in the search for a rule which would fit the case then before the court, and future cases also, doing justice alike to the public and to investors, the fair value rule was announced. It was not intended as a rigid rule which should deprive legislatures and commissions of the right to make rates upon considerations of equity and fair realing. It was intended as a rule which the courts might apply, in particular cases, to prevent confiscation through the enforcement of rates manifestly unjust, in the light of investments made and of all other relevant facts.

The hazards of the business and other special circumstances held by the court below to require inclusion, in the rate base, of the going value item claimed were properly to be considered only as bearing upon the fair rate of return.

The Court below held that a peculiar rule should apply to these gas companies, as to treatment both of the going concern element and of amortization, by reason of the speculative character of the natural gas business, of the fact that in the years when the business of these companies was developed it was unregulated, and of the further fact that the life of natural gas producing properties is rather short. Upon this point the Court said:

> "An allowance for going value is necessitated, due to facts peculiar to this case. In the ordinary public utility case, with no unusual fact or circumstance to affect a court's consideration of it, we assume that going value, as a properly includable item in the rate base, should and would be rejected. * * * Under such circumstances as are here shown, it seems that fairness necessitates the capitalization and inclusion of such skill—aye, and hazards—as legitimately as the cost of pipes. The natural gas was valueless as it lay in Texas wells, four thousand feet beneath the surface of the earth, over one thousand miles from Chicago. What gave it value? Not alone pipes to carry

it, nor pumps to pump it. It was the courage of the investors, and their willingness to take a chance in a speculative venture, the vision to see and to forecast, the integrity of management, and the knowledge of geologists, etc., which gave to the enterprise its life; and the product of these combined factors made for a going value, which, in the realities of the business world, is justly recognized as part of the value of the investment."

We think it is plain that such elements as the difficulties, uncertainties, and hazards which may have attended the establishment of these enterprises are not elements which can properly be appraised and reflected in the rate base, but that such weight as the evidence shows should be attributed to them should have a bearing only upon the fair rate of return which the companies are permitted to earn.

The Court Below Erred in Holding that the Commission's Order Should Be Set Aside Because the Commission Computed the Annual Allowance for Amortization of Capital Assets on the Basis of the Entire Service Life of Such Assets.

The gas companies estimated that their gas reserves will be exhausted prior to the end of 1954. They also estimated that their aggregate investment prior to December 31, 1954, including that heretofore made and hereafter to be made, less salvage, will be $78,284,099. The Commission accepted both estimates.

The companies began operations on January 1, 1932. According to their estimate the total service life of their property will accordingly be twenty-three years. To cover depreciation and depletion they made a claim for an annual amortization allowance to cover the fair value of their property, less salvage, as estimated by them.

The Commission made an amortization allowance based upon the full estimated service life of the property, basing the computation of the same, however, upon the cost of the

properties as estimated by the gas companies, instead of upon their claimed fair value.

The gas companies contend that the amount to be amortized is the fair value of their properties instead of their cost, and that the amortization period should be fourteen years and five months, that being the estimated service life remaining after the effective date of the Commission's rate order. The Court below sustained the companies' contentions.

The commission properly based its amortization allowance upon the entire life of the property to be amortized.

Terming depreciation "amortization" does not call for the application of any new legal principles in its determination or allowance. It is still the amount which should be charged to operating expenses, and collected in rates, in order that the integrity of the owner's investment may be preserved.

It was the duty of the gas companies to make sufficient charges for their service to cover the consumption of their capital while the service was being rendered. *Knoxville* v. *Knoxville Water Co.*, 212 U. S. 1, 13-14; *United R. and E. Co.* v. *West*, 280 U. S. 234, 253; *Lindheimer* v. *Illinois Bell Tel. Co.*, 292 U. S. 151, 167.

The sole justification for the inclusion of an allowance for depreciation in the rates involved is the fact that it is a part of the cost of the service covered by the rates. Such cost is in no way an incident of regulation. It was not non-existent prior to regulation, and is not larger after regulation by reason of the fact that regulation was not imposed from the date of the inception of the enterprise.

The gas companies base their claim for an amortization period less than the service life of the property upon the contention that until the Natural Gas Act was enacted their properties were private properties, that the enactment of the statute constituted a taking of the properties for public use, and that the amortization period used in determining

their compensation thereafter must be limited to the life of the properties after such taking.

We have, earlier in this brief, argued that the gas properties here involved were public utility enterprises, which were at all times subject to public regulation. There was no taking of them for a public use. Their owners voluntarily devoted them to an enterprise which so affects the public interest that the public has a right to regulate them, whenever it deems regulation necessary.

A somewhat strange feature of the gas companies' contention, sustained by the Court below, is the fact that the period of amortization claimed is not even reckoned from the date of the enactment of the Natural Gas Act, when the gas companies maintain that their properties were taken, but is reckoned from the effective date of the Commission's rate reduction order.

It results from the ruling below, assuming the same to be sustained, that the public is penalized for not having earlier deprived the gas companies of complete liberty to charge whatever prices they pleased.

We refrain from making argument that the Constitution imposes no such rule.

The commission properly based its amortization allowance upon the cost of the property to be amortized.

The gas companies contend that the amount to be amortized is the present fair value of their property. They rely upon the opinion of this court in *United R. & E.* v. *West*, 280 U. S. 234, 253. That opinion unquestionably supports their claim. We submit that the opinion is unsound and should be overruled.

The opinion is unsound because it lays down a rule which it is impossible for regulatory commissions to adopt and follow.

Such commissions have been given authority to issue orders, and to require annual or periodic reports, so that the true financial results of the operations of regulated proper-

ties may be readily known to the commissions. Orders prescribing charges which may be made to operating expenses for depreciation must be, accordingly, orders which the regulated companies may understand and comply with, and they must be orders failure to comply with which may be readily observed and proved, so that the commissions can enforce the same.

It is not possible to frame an accounting order, to provide for the charging to operating expenses of depreciation of the various classes of utility property, to be determined upon the basis of the fluctuating cost of reproducing such property, which will enable the regulated companies to know the amounts which they are required to charge, or which can, as a practical matter, be enforced by the commission making the order.

For this reason, we believe it to be true that not a single regulatory commission, Federal or state, has undertaken to conform its order respecting depreciation accounting to the rule laid down in *United R. & E. Co.* v. *West.*

The infirmities of that rule were pointed out in the dissenting opinion of Mr. Justice Brandeis. The almost universal practice in the business world, as, pointed out in that opinion, is to base depreciation charges in accounting upon cost.

In determining the allowance to be made to operating expense in rate cases, it should be kept in mind that the rate proceeding is in no proper sense a determination of an amount to be paid to the owners for the taking of title to their property. It is, in fact, merely a determination, by public authority, of the amount which ought properly to be paid by the public for the services rendered by the enterprise, and covered by the rates to be fixed.

In determining that compensation, workable methods ought to be adopted which reasonably protect the owner and the public. If the practice is followed of charging the cost of property to operating expense in proportion to its consumption, year by year, in conformity with established business usage, the rights of both the public and the owner will be protected.

Under the *Smyth* v. *Ames* opinion, among the matters to be considered and attributed proper weight by a regulatory agency is "the sum required to meet operating expenses." To enable such expenses to be estimated for consideration, it must be open to the rate-making agencies to compute the same upon some rational and practicable basis. We maintain that if the rate-making agency, in the exercise of its judgment, adopts a method for determining the expense of annual depreciation which accords with the common practice of the business world, it is within the *Smyth* v. *Ames* rule, and that its determination can not properly be held arbitrary or otherwise unconstitutional by any reviewing Court.

If the commission's order was made after a due process of law hearing, the only question open for the consideration of the Court is whether the rates prescribed are confiscatory.

If the Commission's order was made after a due process of law hearing, the only question open for the consideration of the Court is whether the rates prescribed are confiscatory.

The principle applicable to the determination of that question has been clearly announced by this Court. The fixing of rates is a legislative act. In exercising its rate making function Congress, or a State legislature, has a broad discretion. It may exercise its authority directly or through an agency vested with jurisdiction to act, for that purpose, in accordance with the broad standard of justice and reasonableness, ordained by the legislative power.

The Court does not sit as a board of review, to substitute its judgment for the judgment of such agencies, when acting within the field assigned to them by the legislative power.

> "In such cases, the judicial inquiry into the facts goes no further than to ascertain whether there is evidence to support the findings, and the question of the weight of the evidence in determining issues of fact

lies with the legislative agency acting within its statutory authority." *St. Joseph Stockyards Co.* v. *United States*, 298 U. S. 38, 50-51; *Los Angeles Gas and Elec. Corp.* v. *The Railroad Commission*, 289 U. S. 287, 304.

See also, as to the finality of determinations by administrative agencies, when acting under legislative grants of authority, *National Labor Relations Board* v. *Link Belt Co.*, U. S. , Jan. 6/41; *Gray, Director* v. *Receivers of Seaboard Airline Railway*, U. S. , December 15, 1941.

Congress has ordained that the rates of natural gas companies shall be just and reasonable, and has made the Commission its ageney to determine what rates fall within that standard, and to enforce the same by orders. The Commission accordingly had jurisdiction to require unreasonably high rates to be reduced.

The gas companies contend, however, that, even though 6½ percent be held a nonconfiscatory rate of return, yet the evidence does not show their rates, which produce a return exceeding that percentage, to be unreasonable. Hence they maintain the Commission's order requiring reduction to be beyond its authority.

Assuming that there is, or may be, a difference between the level of rates which are barely nonconfiscatory and those which are reasonable, in a given case, the only question which this Court may consider, when reviewing a rate order of the Commission, is whether the rates challenged meet the constitutional standard. Whether, upon the record, it is reasonable that something more than a nonconfiscatory return be permitted, and if so how much more, are not questions for the Court. Those are questions of fact, which Congress has left to the Commission, and with respect to which it has made the Commission's finding conclusive, by the express provision of Section 19(b) of the Natural Gas Act.

In the record in this case, there was substantial evidence to support the Commission's findings as to rate base, fair rate of return, and reasonableness of rates. The Commis-

sion had before it evidence as to the original cost of properties, their reproduction cost, the "viewed depreciation," the claim of the gas companies as to the amount of annual amortization, the service life of properties, the length of time they had been in service, the financial results of such operation, a full financial history of the properties, and much evidence as to fair rate of return.

Counsel for the gas companies urge, however, that the percentage of return produced by rates upon the rate base value is no evidence whatever as to the reasonableness of the rates which produce that return, and that, hence, the Commission's findings that the existing rates are unjust and unreasonable is unsupported by substantial evidence, and that its order based upon that finding should be set aside on that ground.

We concede that the rate of return which is fair for a given enterprise may depend upon many circumstances, but when that rate has been determined, and applied to a properly determined rate base, it is a conclusive test as to the reasonableness of rates,—subject to the principle, always applicable, that the owner of a public service enterprise may never exact from the public more for any service than such service is fairly worth. In this case the facts respecting the character of the enterprise, the difficulties and hazards alleged to be incident to its establishment were before the Commission, together with such other evidence bearing upon the question of a fair rate of return as the gas companies desired to offer. Upon the consideration of such evidence the Commission determined 6½ percent to be a fair rate of return upon the rate base fixed. This generous return may be contrasted with barely more than 5 percent, held to be a nonconfiscatory return for the company which performs a share of the very public service enterprise in which these gas companies are engaged by distributing to consumers the gas which they sell for resale. *Peoples Gas Light and Coke Co.* v. *Hart et al.*, 367 Ill. 435, 287 Ill. App. 379, 373, Ill. 31, 309 U. S. 634.

If the fair rate of return so fixed meets the constitutional standard the question whether it, at the same time, meets

the standard of reasonableness required by the Natural Gas Act is foreclosed by the finding of the Commission.

The ruling in Cotting v Godard, even if admitted to be sound for application in any case, could not be applied in the administration of the natural gas act without defeating the purpose of the act.

Counsel for the gas companies cite *Cotting* v. *Godard*, 183 U. S. 79 and other cases claimed to support the principle that rates may not be found to be unreasonable except upon evidence that they exceed the value of the services covered by the same to those who receive such services.

Refraining from discussing the soundness of the ruling in *Cotting* v. *Godard*, for application in any case, and likewise from an examination of subsequent cases, whereby it might be demonstrated that the principle announced in that case has not been adopted and followed in this country, we point out that the rates of gas utilities, for gas sold for resale, can not possibly be tested, as to their reasonableness, by the value of the service to the purchasers, for the reason that such gas service, to the purchasing companies, are ordinarily worth whatever such companies are permitted to be charged. This is true because they do not themselves consume the gas supplied, but merely share in the joint enterprise of distributing the same to the public. The amounts which are permitted to be charged to them are operating expenses which are passed along to the public. So long as the charges exacted from them do not so increase the prices which they are compelled to charge the public that their business is restricted and rendered less profitable, it can not be said that the rates exacted from them exceed the value to them of the services they receive.

If the effect of the rates upon the distributing companies should be made the determining test as to the reasonableness of such rates, in the administration of the Natural Gas Act, the prime purpose of the Act, which is protection of the ultimate consumers, would be defeated.

The gas companies should refund to their customers the overcharges which have been made since the effective date of the commission's order.

Counsel for the gas companies have argued in their briefs that even if the judgment below shall be reversed, and the Commission's order shall be sustained, they should not be required to refund to their customers the excess rates which have been collected from the effective date of the Commission's order. Their argument is that if they shall be required to pay such excess to their customers it can not by any action of the State commissions be passed on to the ultimate consumers, and that such payment will result only in "transferring this money to the pockets of the distributing utilities, thus enriching the utilities at the expense of cross-petitioners, with no benefit whatever accruing to the ultimate consumers of the utilities, for the protection of whose interests the legislation was enacted."

To this argument it would seem a sufficient reply to suggest that if the rates the gas companies have been collecting were unreasonably high and, as to such excess, unlawful, under Section 4(a) of the Natural Gas Act, and violative of a valid order of the Commission, to permit them to retain the unlawful excess would leave in their hands what does not belong to them, and would result in their unjust enrichment.

The amount of this excess is great, amounting to more than $10,000 per day for all the time the gas companies have been able to delay the enforcement of the Commission's order. If such large amounts are permitted to accrue to gas companies as benefits resulting from the mere prolongation of litigation, wholly without legal justification, it may not be expected that any rate reduction order of the Commission will ever be permitted to become effective till litigation concerning it has been extended to the utmost limits which the ingenuity of counsel shall make, possible, nor may any such litigation be regarded as unsuccessful, from the point of view of the gas companies, notwithstand-

ing the final establishment of the validity of the orders litigated.

It ought not, however, to be assumed that the courts and regulatory commissions are impotent to deal with a situation such as arises when a natural gas company asserts its right to ask for a judicial review of an order of the Federal Power Commission reducing its rates. What has been done here, other than the action taken by the Court of Appeals in connection with the granting of an injunction, and the requirement of a bond intended to require a refund in the event the order now before the Court shall be sustained, does not appear from this record. There is, however, no reason for assuming that nothing has been done.

The Commission's order when made was presumptively lawful. Suspension of its enforcement by injunction was accompanied by the action taken by the Court to require the refund now under discussion. For aught that appears in this record, the State commission may have reflected the reduction ordered in reduced rates, prescribed for distributing companies. In such case, the distributing companies may have put the reductions into effect, or they, too, may have obtained stay orders, from the State courts, pending the determination of litigation involving the validity of such reduction orders, filing bonds in connection therewith conditioned to make appropriate refunds to ultimate consumers, if the rate reduction orders shall be finally sustained.

In any event this Court will not guess about what has happened since the Commission's order here involved was made. The excess which the gas companies have collected does not belong to them. As between them and their customers, from which they have unlawfully collected it, the excess belongs to those customers. Whether, as between such customers and the ultimate consumers, such excess belongs equitably to the ultimate consumers, and if so, what, if anything, can be done to secure the enjoyment of it by them, are questions not before this Court in these proceedings.

CONCLUSION.

Counsel for the gas companies in their brief have argued various other alleged grounds of illegality of the Commission's order, not touched upon in this brief, which we believe to be groundless. As to those, however, there is nothing which we desire to urge additional to what has already been said in the brief on behalf of the Federal Power Commission and the Illinois Commerce Commission, heretofore filed.

Respectfully submitted on behalf of the National Association of Railroad and Utilities Commissioners,

JOHN E. BENTON,
General Solicitor of said Association.

January 12, 1942

SUPREME COURT OF THE UNITED STATES.

Nos. 265, 268.—October Term, 1941.

Federal Power Commission and Illinois Commerce Commission, Petitioners,
265 *vs.*
Natural Gas Pipeline Company of America and Texoma Natural Gas Company.

Natural Gas Pipeline Company of America and Texoma Natural Gas Company, Petitioners,
268 *vs.*
Federal Power Commission and Illinois Commerce Commission.

On Writs of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.

[March 16, 1942.]

Mr. Chief Justice Stone delivered the opinion of the Court.

This is a rate case involving numerous questions which arise out of the Federal Power Commission's regulation, under §§ 5(a) and 13 of the Natural Gas Act of 1938, 52 Stat. 821, 15 U. S. C. § 717, of the rates to be charged for the sale of natural gas by cross-petitioners, Natural Gas Pipeline Company of America and Texoma Natural Gas Company.

The two companies are engaged in business as a single enterprise. They produce natural gas from their own reserves in the Panhandle gas fields in Texas, and purchase gas produced there by others. They transport the gas by their own pipeline in interstate commerce to Illinois, where they sell the bulk of it at wholesale to utilities, which distribute and sell it for domestic, commercial and industrial uses.

The companies began operations in 1932 with a capital structure of $60,000,000 of six per cent bonds, later increased by $999,000, and $2,500,000 of common stock, of which $500,000 is stock of the Texoma Company, a non-profit corporation paying no divi-

dends on its stock. During the first seven years of operation, beginning January 1, 1932, and extending through 1938, the companies charged to gross income various depreciation and depletion deductions aggregating $13,077,488,[1] and in addition charged $6,481,322 for "retirements" of property. In that period they paid dividends amounting in all to $9,150,000. Although there were book deficits in earnings for the first two years, the total "net profit" available for dividends and surplus after payment of interest on the bonds was $8,224,436,[2] or an annual average of $1,174,919, which is 33.6% per annum on the $3,500,000 stock. The earnings available during the period for return on the capital investment of both stockholders and bondholders — after taking out of income $19,558,810 for depreciation, depletion and retirements — totalled $34,040,883; this makes an average of $4,862,983 annually, which is about 8% on the book figures for investment undepreciated, or 8.8% after deducting from investment the average depreciation and depletion reserves actually charged to earnings by the companies.[3] At the time of the hearing, over one-fourth of the bonds issued had been retired out of earnings.

On complaint of the Illinois Commerce Commission, and on its own motion, the Power Comission began separate investigations of the companies' rates. These proceedings were consolidated and after extensive hearings the Commission, for the purpose of issuing an interim order, accepted the companies' statement that the book cost of their property existing at the end of 1938 was $60,172,843, including working capital of $975,000. Likewise for the purpose of the order, it accepted the companies' estimate that the value of all physical property—calculated at reproduction cost new (except for gas reserves taken on the companies' statement to have a present value of $13,334,775)—was $74,420,424, which the Commission adopted as the rate base. It took the companies'

[1] These charges against income are slightly in excess of the accumulated reserves for depreciation and depletion—$12,557,892—shown by the books at the end of 1938. The excess of $519,596 is apparently due to the fact that during the period $7,000,918 of property, on the basis of book cost, was retired, while the annual retirement charges had aggregated only $6,481,322. The balance of the retirements, $519,596, apparently had been charged to the depreciation and depletion accounts.

[2] This includes a negligible item, "non-operating income", which for the seven-year period came to only $194,600.

[3] The book figures (which are on a cost basis) for invested capital average slightly under $61,000,000 if working capital is included. The depreciation and depletion reserves are taken from the accounts for which the aggregate figure, $12,357,892, is given in note 1, *supra*.

own estimate of twenty-three years ending in 1954 as the life of the business, and for the amortization base used their cost figure of $78,284,009 for the total past and estimated future investment after deduction of estimated salvage. It calculated the "annual amortization expense" on that amount for the twenty-three year period, at a 6½% sinking fund interest rate, as $1,557,852, which it allowed.

The Commission also accepted, for the purpose of its interim order, the companies' estimate of prospective income available for amortization and return for the period 1939 to 1942 inclusive, as averaging $9,511,454 per annum. But making allowance for higher income tax rates under the Revenue Act of 1940, it found that the income available for amortization and return would be decreased to $9,362,032. It concluded that the companies' estimate of return, less the amortization allowance, ($9,362,032 less $1,557,852), —or $7,804,180—exceeded the fair return, $4,837,328 (which is 6½% of the rate base of $74,420,424), by $2,966,852, which amount was available for reduction of net revenues. Taking into account the decrease of $783,909 in federal income taxes which would result from such a decline in revenues, the Commission decided there was a total of $3,750,000 annually available for reduction of rates. It found the existing rates were "unjust, unreasonable and excessive", and made its interim order directing the companies to file a new schedule of rates and charges effective after September 1, 1940, which would bring about an annual reduction of $3,750,000 in operating revenues. The order also provided that the record should "remain open" for such further proceedings as the Commission may deem necessary or desirable.

On the companies' petition for review of the order pursuant to § 19(b) of the Act, the Court of Appeals for the Seventh Circuit, 120 F. 2d 625, upheld the validity of the rate regulation provisions of the Act, and the Commission's authority under the statute to issue the interim order directing reduction of the rates and requiring respondents to file new schedules reflecting that reduction. But the court vacated the Commission's order on the sole grounds that "going concern value" to the extent of $8,500,000 should have been included in the rate base, and that the amortization period for the entire property, instead of the full twenty-three year estimated life of the business taken by the Commission, should have been dated from the passage of the Act or the time of the Commission's order.

We granted certiorari, 314 U. S. —, because of the novelty and importance of the questions presented upon the Commission's petition challenging the grounds of reversal below, and on the companies' cross petition assailing the constitutionality of the Act, the authority of the Commission to make the interim order, the prescribed 6½% return, the computation of the amortization allowance on the same rate of interest as the fair rate of return, and other features of the Commission's order presently to be discussed.

The Natural Gas Act declares that "the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest", and that federal regulation of interstate commerce in natural gas "is necessary in the public interest". § 1(a). The Act directs that all rates and charges in connection with the transportation or sale of natural gas, subject to the jurisdiction of the Commission, shall be "just and reasonable" and declares to be unlawful any rate or charge which is not just and reasonable. § 4(a). By § 5 the Commission, on its own motion or the complaint of a state, municipality, state commission or gas distributing company, is empowered to investigate the rates charged by any natural gas company in connection with any transportation or sale of any natural gas subject to the jurisdiction of the Commission, and after a hearing to determine just and reasonable rates.

Constitutionality of the Act. The argument that the provisions of the statute applied in this case are unconstitutional on their face is without merit. The sale of natural gas originating in one state and its transportation and delivery to distributors in any other state constitutes interstate commerce, which is subject to regulation by Congress. *Illinois Natural Gas Co.* v. *Central Illinois Pub. Serv. Co.*, 314 U. S. —. It is no objection to the exercise of the power of Congress that it is attended by the same incidents which attend the exercise of the police power of a state. The authority of Congress to regulate the prices of commodities in interstate commerce is at least as great under the Fifth Amendment as is that of the states under the Fourteenth to regulate the prices of commodities in intrastate commerce. Compare *United States* v. *Carolene Products Co.*, 304 U. S. 144; *United States* v. *Rock Royal Co-op.*, 307 U. S. 533, 569; *Sunshine Coal Co.* v. *Adkins*, 310 U. S. 381, 393-97; *United States* v. *Darby*, 312 U. S. 100, with *Nebbia* v. *New York*, 291 U. S. 502; *Olsen* v. *Nebraska*, 313 U. S. 236.

The price of gas distributed through pipelines for public consumption has been too long and consistently recognized as a proper subject of regulation under the Fourteenth Amendment to admit of doubts concerning the propriety of like regulation under the Fifth. *Willcox* v. *Consolidated Gas Co.*, 212 U. S. 19; *Cedar Rapids Gas Co.* v. *Cedar Rapids*, 223 U. S. 655; *Railroad Commission* v. *Pacific Gas Co.*, 302 U. S. 388. And the fact that the distribution here involved is by wholesale rather than retail sales presents no differences of significance to the protection of the public interest which is the object of price regulation. Cf. *Illinois Nat. Gas Co.* v. *Central Illinois Pub. Serv. Co.*, *supra*. The business of cross-petitioners is not any the less subject to regulation now because the Government has not seen fit to regulate it in the past. Cf. *Nebbia* v. *New York*, *supra*, 538-39.

Validity of the Interim Order. The companies contend that the Federal Power Commission has no authority under the Act to enter the type of order now under review, and that the order is invalid because the Commission did not itself fix reasonable rates as required by the Act but instead merely directed the companies to file a new rate schedule which would result in the prescribed reduction in operating revenues. Section 5(a) of the Act provides: "Whenever the Commission, after a hearing . . . , shall find that any rate . . . is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate . . . and shall fix the same by order". It also contains a proviso that the Commission shall not have power to order an increase of rates on file unless in accordance with a new schedule filed by the company. But without mention of new rate schedules the proviso adds that the Commission "may order a decrease where existing rates are unjust . . . or are not the lowest reasonable rates". And § 16 gives the Commission "power to . . . issue . . . such orders . . . as it may find necessary or appropriate to carry out the provisions of this Act".

The first prerequisite to an order by the Commission is that it shall be preceded by a hearing and findings. In this case, while the proceedings were not ended by the interim order, the companies had full opportunity to offer all their evidence both direct and in rebuttal, and full opportunity to cross-examine every witness offered by both the Federal Power Commission and the Illinois Commerce Commission. All the evidence tendered was received and considered by the Commission, and before the interim

order was entered counsel for the companies stated to the Commission that they had concluded the direct testimony in support of their case. So far as the order is supported by the evidence the companies cannot complain that they were denied a full hearing because they had not been able to examine on redirect their own witnesses who had not been cross-examined, or because they had no opportunity to cross-examine or rebut witnesses who were not offered by the Commission. The right to a full hearing before any tribunal does not include the right to challenge or rely on evidence not offered or considered. See *New England Divisions Case*, 261 U. S. 184, 201.

The establishment of a rate for a regulated industry often involves two steps of different character, one of which may appropriately precede the other. The first is the adjustment of the general revenue level to the demands of a fair return. The second is the adjustment of a rate schedule conforming to that level so as to eliminate discriminations and unfairness from its details. Such an orderly procedure for establishing the rates prescribed by the Act would seem to be an appropriate means of carrying out its provisions. Section 5 of the Act was modelled on the provisions of the Transportation Act, 49 U. S. C. §§ 13, 15, which have been interpreted as giving to the Interstate Commerce Commission authority to establish a general level of rates and divisions in advance of a schedule to be filed by the carriers. See *New England Divisions Case, supra*, 201-02, 203, n. 21. Cf. Sharfman, The Interstate Commerce Commission, vol. 2, pp. 381-82; *Driscoll* v. *Edison Co.*, 307 U. S. 104.

We think that the proviso of § 5 already quoted contemplates that, when existing rates are found to be unjust and unreasonable, an order decreasing revenues may be filed without establishing a specific schedule of rates. Since such an order may be in the interests of the public, as well as the regulated company, and is in harmony with the purposes of the Act, it is one which the Commission has discretion to make under § 16 as appropriate to carry out the provisions of the Act.

The Scope of Judicial Review of Rates Prescribed by the Commission. The ultimate question for our decision is whether the rate prescribed by the Commission is too low. The statute declares, § 4(a), that the rates of natural gas companies subject to the Act "shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful". Section 5(a)

directs the Commission to "determine the just and reasonable rate" to be observed and requires the Commission to "fix the same by order". It also provides that "the Commission may order a decrease where existing rates are unjust . . . unlawful, or are not the lowest reasonable rates". On review of the Commission's orders by a Circuit Court of Appeals as authorized by § 19(b), the Commission's findings of fact "if supported by substantial evidence, shall be conclusive".

By long standing usage in the field of rate regulation the "lowest reasonable rate" is one which is not confiscatory in the constitutional sense. *Los Angeles Gas Co.* v. *Railroad Commission*, 289 U. S. 287, 305; *Railroad Commission* v. *Pacific Gas Co., supra*, 394, 395; *Denver Stock Yard Co.* v. *United States*, 304 U. S. 470, 475. Assuming that there is a zone of reasonableness within which the Commission is free to fix a rate varying in amount and higher than a confiscatory rate, see *Benton* v. *Belt Line Ry.*, 268 U. S. 413, 422, 423; *Columbus Gas Co. v. Commission*, 292 U. S. 398, 414; *Denver Stock Yard Co.* v. *United States, supra*, 483, the Commission is also free under § 5(a) to decrease any rate which is not the "lowest reasonable rate". It follows that the Congressional standard prescribed by this statute coincides with that of the Constitution, and that the courts are without authority under the statute to set aside as too low any "reasonable rate" adopted by the Commission which is consistent with constitutional requirements.

The Constitution does not bind rate-making bodies to the service of any single formula or combination of formulas. Agencies to whom this legislative power has been delegated are free, within the ambit of their statutory authority, to make the pragmatic adjustments which may be called for by particular circumstances. Once a fair hearing has been given, proper findings made and other statutory requirements satisfied, the courts cannot intervene in the absence of a clear showing that the limits of due process have been overstepped. If the Commission's order, as applied to the facts before it and viewed in its entirety, produces no arbitrary result, our inquiry is at an end.

Going Concern Value. The companies insist that their business has a going concern value of $8,500,000 which the Commission did not include in the rate base and on which they are entitled to earn a return. In establishing the rate base for the

purposes of the interim order the Commission "reluctantly" accepted the estimates of value, presented by the companies' own witnesses, as follows:

Reproduction Cost New of Physical Properties (exclusive of Gas Reserves)	$56,302,250[4]
Value of Gas Reserves as of June 1, 1939	13,334,775
Capital Additions from June 1, 1939, to December 31, 1942	3,808,399[5]
Working Capital	975,000
Total Rate Base	$74,420,424

While no item for going concern value is separately stated in the rate base, the computation of cost new of physical equipment included—in addition to labor and cost of materials—large amounts for overhead, interest, taxes, administration, legal and supervisory charges, and expenses paid or incurred in assembling the plant as that of a going concern.

The Commission spoke of the rate base thus arrived at as "liberal" and as a "generous allowance". That the estimate of reproduction costs new is liberal is indicated by the circumstances that the companies' structures other than gas reserves were built in 1930-1931 at a time, as the record shows, of relatively high prices, and that their reproduction cost depreciated is greater than actual cost, which was about $50,000,000. And the allowed "present value" of leases as of June 1, 1939, $13,334,775, is approximately $4,000,000 more than book cost, even without taking into account a substantial reduction for depletion reserves of $1,152,854, which the companies had accrued on their own books by the end of 1938. The Commission declined to include going concern value as an additional item in the rate base.

[4] The estimates submitted by the companies stated that there should be deducted from this figure for "viewed depreciation" $2,866,758. However, in setting a rate base for the interim order, the Commission did not make this conceded deduction—perhaps because it held, contrary to the companies' contention, that the properties should be amortized over the entire life of the business.

[5] The companies estimated that the cost of additional property, not including replacements, during the future life of the enterprise, subsequent to June 1, 1939, would be $9,145,083. On this basis, they claimed that there should be included in the rate base $6,046,286, which they said would be the estimated average investment. The Commission included in the rate base only $3,808,399, which was the companies' estimated outlay for capital additions through the end of 1942. This reduction does not appear to be challenged. In any event, the refusal to include in the rate base capital expenditures not yet made can not involve confiscation.

The companies urge, as the Court of Appeals held, that there are items of cost or expense incurred in the establishment and development of the business during the seven-year period prior to regulation which were not included in the companies' estimate of value accepted by the Commission and which, in view of the special characteristics of the business, should be capitalized and added to the rate base to the extent of $8,500,000 for going concern value. They include, in amounts not now material, the following: expenditures for securing new business; interest on money invested in non-productive plant capacity; taxes paid on non-productive capacity; fixed operating expenses attributable to non-productive capacity, and depreciation on non-productive capacity.[6] The companies' contentions with respect to all these items are predicated upon the limited life of the business, twenty-three years, and on testimony that in anticipation of its growth larger gas mains and facilities were constructed than were required during the earlier years of the business. The reproduction cost new of this excess of equipment is admittedly included in the rate base.

None of these items appears in the companies' capital account. With the possible exception of expenditures for securing new business, they are synthetic figures arrived at by estimating the amount of expense attributable to the current cost of maintenance of the excess capacity of the plant during periods when the excess capacity was not used. But the interest charges, taxes and other costs of maintaining this excess capacity during the period when not in use have not been capitalized by the companies on their books and so far as appears were paid from current earnings. The same is true of the expenditure for advertising and other expenses of acquiring new business.

The novel question is thus presented whether confiscation, proscribed by Congress as well as the Constitution, results from the exclusion from the rate base of the previous costs of maintaining excess plant capacity and of getting new business. The Commission gave full consideration to this contention. It said: "The companies' claim for $8,500,000 for 'going concern value must be disallowed. The amount obviously is an arbitrary claim, not supported by substantial evidence warranting its al-

[6] The item for depreciation on non-productive capacity amounting to $382,833 is obviously provided for in the Commission's allowance for depreciation. The value of the companies' entire plant, whether fully productive or not, is included in the rate base and, as will presently appear, provision was made by the Commission's order for its amortization on a cost basis from earnings.

lowance. Its allowance would mean the acceptance of a deceptive fiction, resulting in an unfair imposition upon consumers. We are convinced that we are allowing in our rate base more than an adequate amount to cover all elements of value."

There is no constitutional requirement that going concern value, even when it is an appropriate element to be included in a rate base, must be separately stated and appraised as such. This Court has often sustained valuations for rate purposes of a business assembled as a whole without separate appraisal of the going concern element. *Columbus Gas Co.* v. *Commission*, 292 U. S. 398, 411; *Dayton P. & L. Co.* v. *Commission*, 292 U. S. 290, 309; *Denver Stock Yard Co.* v. *United States, supra*, 478-80; *Driscoll* v. *Edison Co., supra*, 117. When that has been done the burden rests on the regulated company to show that this item has neither been adequately covered in the rate base nor recouped from prior earnings of the business. *Des Moines Gas Co.* v. *Des Moines*, 238 U. S. 153, 166.

The total value of the companies' plant, including equipment in excess of immediate needs when beginning business, has been included in the rate base adopted. If rightly included, as the Commission has assumed for purposes of the order, the companies would have been entitled to earn a fair return upon its value, had the business been regulated from the start. But it does not follow that the companies' property would be confiscated by denying to them the privilege of capitalizing the maintenance cost of excess plant capacity, which would allow them to earn a return and amortization allowance upon such costs during the entire life of the business. It is only on the assumption that excess capacity is a part of the utility's equipment used and useful in the regulated business, that it can be included as a part of the rate base on which a return may be earned. When so included the utility gets its return not from capitalizing the maintenance cost, but from current earnings by rates sufficient, having in view the character of the business, to secure a fair return upon the rate base provided the business is capable of earning it. But regulation does not insure that the business shall produce net revenues, nor does the Constitution require that the losses of the business in one year shall be restored from future earnings by the device of capitalizing the losses and adding them to the rate base on which a fair return and depreciation allowance is to be earned.

Galveston Electric Co. v. *Galveston*, 258 U. S. 388; *San Diego Land & Town Co.* v. *Jasper*, 189 U. S. 439, 446-47. The deficiency may not be thus added to the rate base for the obvious reason that the hazard that the property will not earn a profit remains on the company in the case of a regulated, as well as an unregulated business.

Here the companies, though unregulated, always treated their entire original investment, together with subsequent additions, as capital on which profit was to be earned. They charged the out-of-pocket cost of maintenance of plant, whether used to capacity or not, as operating expenses deductible from earnings before arriving at net profits. They have thus treated the items now sought to be capitalized in the rate base as operating expenses to be compensated from earnings, as in the case of regulated companies. The history of the first seven years of operation before regulation shows an average annual return,[7] after deduction of operating expenses, of approximately 8% on the undepreciated investment. This high return was earned during a period which included the severest depression in our history.

Whether there is going concern value in any case depends upon the financial history of the business. *Houston* v. *Southwestern Tel. Co.*, 259 U. S. 318, 325. This is peculiarly true of a business which derives its estimates of going concern value from a financial history preceding regulation. That history here discloses no basis for going concern value, both because the elements relied upon for that purpose could rightly be rejected as capital investment in the case of a regulated company, and because in the present case it does not appear that the items, which have never been treated as capital investment, have not been recouped during the unregulated period.

We cannot say that the Commission has deprived the companies of their property by refusing to permit them to earn for the future a fair return and amortization on the costs of maintenance of initial excess capacity—costs which the companies fail to show have not already been recouped from earnings before computing the substantial "net profits" earned during the first seven years. The items for advertising and acquiring new business have been treated in the same way by the companies and do not in the

[7] Besides $8,244,435 of "net profits", the companies paid out of gross income $23,294,030 as interest on the bonds.

circumstances of this case stand on any different footing. Cf. *West Ohio Gas Co.* v. *Commission*, 294 U. S. 63, 72.

The Amortization Base. The Commission took as the amortization base the sum of $78,284,009. This was made up of the companies' total investment, at the end of 1938, of $67,173,761 (without deduction of property retirements already made), plus estimated future capital additions through 1954, including replacements, amounting to $12,159,380,[8] less estimated salvage at the predicted end of the project in 1954. It is not questioned that the Commission's annual amortization allowance of $1,557,852, accumulated at the sinking fund interest rate of 6½% adopted by the order, will be sufficient in 1954 to restore the capital investment so computed.

The companies argue that the amortization base, computed on a basis of reproduction cost, should be $84,341,218[9] rather than cost plus estimated future capital additions. But the purpose of the amortization allowance and its justification is that it is a means of restoring from current earnings the amount of service capacity of the business consumed in each year. *Lindheimer* v. *Illinois Tel. Co.*, 292 U. S. 151, 167. When the property is devoted to a business which can exist for only a limited term, any scheme of amortization which will restore the capital investment at the end of the term involves no deprivation of property. Even though the reproduction cost of the property during the period may be more than its actual cost, this theoretical accretion to value represents no profit to the owner since the property dedicated to the business, save for its salvage value, is destined for the scrap-heap when the business ends. The Constitution does not require that the owner who embarks in a wasting-asset business of limited life shall receive at the end more than he has put into it. We need not now consider whether, as the Government urges, there can in no cir-

[8] We do not intimate any approval of the inclusion in the amortization base of all the estimated future capital additions.

[9] The companies' proposed amortization base was made up of the following items:

Reproduction cost new, exeluding gas reserves	$56,302,250
Viewed depreciation (deduct)	2,866,758
Value of gas reserves	13,334,775
Cost of additional property	9,145,083
Going concern value	8,500,000
Working capital	975,000
	$85,390,350
Less salvage	1,049,132
	$84,341,218

cumstances be a constitutional requirement that the amortization base be the reproduction value rather than the actual cost of the property devoted to a regulated business. Cf. *United Railways* v. *West*, 280 U. S. 234, 265. It is enough that here the business by hypothesis will end in 1954, and that the amortization base, computed at cost and including property already retired, will be completely restored by 1954 by the annual amortization allowances. As the Commission declared: "The amounts of amortization are recognized and treated as operating expenses. Operating expenses are stated on the basis of cost. . . . We refuse to make an allowance of amortization in excess of costs. To do so would not be the computation of a proper expense, but instead the allowance of additional profit over and above a fair return. Manifestly such an additional return would unjustly penalize consumers."

The Amortization Period. The court below held that, since the business was unregulated for the first seven years, the adoption by the Commission of the estimated twenty-three year life of the business as the amortization period involved a denial of due process. In view of the estimate by the Commission and the companies that the gas properties would be exhausted in about sixteen years from the date of the Act, the court thought, as the companies argue, that a rate of return would be confiscatory which would not provide, in addition to a fair return, an annual amortization allowance sufficient to restore the total investment over the final sixteen-year period. But this argument overlooks the fact that the depreciation of physical property attributed to use, and the obsolescence of the entire property attributable to lapse of time in the case of a business having a limited life, had been taking place during the seven years before regulation and that those items must be recouped if at all from earnings. Capital investment loss at the end of the life of a business can only be avoided by restoration of the investment from earnings, and is avoidable so far as is humanly possible only by an appropriate charge of amortization to earnings as they accrue.

Here there is no question but that the Commission's annual amortization allowance, if applied over the entire twenty-three year life of the business, is sufficient to restore the total capital investment at the end, or that earnings of the past and those estimated for the future together are sufficient to provide for the amortization allowance and a fair return, given an appropriate rate base and rate of return. Making that assumption we cannot

say that adequate provision has not been made for restoration of the companies' investment from earnings and a fair return on the investment. Even though the companies were unregulated for seven years, earnings during that period were available and adequate for amortization. In fact the companies' charges to earnings, for depreciation, depletion and retirements, totalled $19,558,810, or an average of $2,794,115 per annum. This was in conformity with the established business practice, in the case of unregulated as well as regulated businesses, to make such a depreciation or amortization allowance chargeable annually to earnings as an operating expense in order to provide adequately for annual consumption of capital in the business. *Lindheimer* v. *Illinois Tel. Co., supra.*

The companies are not deprived of property by a requirement that they credit in the amortization account so much of the earnings received during the prior period as are appropriately allocable to it for amortization. Only by that method is it possible to determine the amount of earnings which may justly be required for amortization during the remaining life of the business.

Amortization Interest Rate. The annual amortization allowances of $1,557,852, if accumulated at a 6½% compound interest rate until the assumed exhaustion of the gas reserves in 1954, will be sufficient to restore the undepreciated total investment less the salvage value of the property. The companies urge that the interest rate should have been lower, say 2%, on the assumption that only some such lower rate would be earned by a hypothetical sinking fund to be created from the annual amortization allowances. But the argument ignores the fact that the amortization method adopted by the Commission contemplates not a sinking fund of segregated securities purchased with cash withdrawn from the business, but merely a sinking fund reserve charged to earnings and not distributable as ordinary dividends. Under this method there is no deduction of the amortization allowances from the rate base on which a fair return—6½% under the current interim order—is to be allowed during the life of the business.

The companies are thus allowed to earn in each year, in addition to the amortization allowance, 6½% on both the amortized and the unamortized portions of the base. If the amortization interest were computed at a 2% rate without deducting the amortized portion from the rate base, the companies would continue to receive a 6½% instead of only a 2% return on that portion of the investment. True, the method of amortization adopted means that

the companies look to the earnings of the business for the hypothetical interest on amortization reserve. This it is argued may involve more business risk than a method of amortization contemplating the actual withdrawal from the business of the amortization allowances and their investment in segregated securities bearing a lower rate of interest. But here the 6½% rate of return allowed on the amortized portion of the rate base includes compensation for the business risk, and the risk is an incident of the business in which the companies have hazarded their capital and in which they propose to invest additional capital. The Commission declared it adopted this method to avoid the inequitable result which would follow if the companies were permitted to include in their charges to the public 6½% on the amortized portion of the base, while treating it as earning only 2%. The Commission's conclusion that this is an appropriate method is supported by the evidence, and in any case it does not appear that it has deprived or will deprive the companies of property.

Fair Rate of Return. The Commission found that "6½ per cent is a fair annual rate of return upon the rate base allowed", which it had characterized as "a generous allowance". The courts are required to accept the Commission's findings if they are supported by substantial evidence. § 19(b). We cannot say on this record that the Commission was bound to allow a higher rate.

The evidence shows that profits earned by individual industrial corporations declined from 11.3% on invested capital in 1929 to 5.1% in 1938. The profits of utility corporations declined during the same period from 7.2% to 5.1%. For railroad corporations the decline was from 6.4% to 2.3%. Interest rates were at a low level on all forms of investment and among the lowest that have ever existed. The securities of natural gas companies were sold at rates of return of from 3% to 6% with yields on most of their bond issues between 3% and 4%. The interest on large loans ranged from 2% to 3.25%.

The regulated business here seems exceptionally free from hazards which might otherwise call for special consideration in determining the fair rate of return. Substantially all its product is distributed in the metropolitan area of Chicago, a stable and growing market, through distributing companies which own 26%

of the investment of the Natural Gas Pipeline Company. Ninety per cent of its gas is taken under contract by the Chicago District Pipeline Company. The contract runs until 1946 or until 1951, at the option of the companies. Under it the District Company is bound to take, or at least pay for, 66-2/3% of the companies' gas, and performance is guaranteed by the three companies distributing the gas in Chicago.

The danger of early exhaustion of the gas field was fully taken into account in the estimate of its life and the companies' estimate was accepted. Provision for the complete amortization of the investment within that period affords a security to the investment which is lacking to those industries whose capital investments must be continued for an indefinite period. The companies' affiliation with the six large corporations which directly or indirectly own all the stock places them in a strong position for their future financing. The business is in the same position as other similar businesses with respect to increased taxation, inflation and costs of operation. Other factors such as credit risks, risks of technological changes, varying demands for product, relatively small labor requirements, and conversion of inventory into cash compare more favorably. After a full consideration of all of these factors and of expert testimony, the Commission concluded that the prescribed reduction in revenues was just and reasonable, and that the 6½% was a fair rate of return.

Disposition of Excess Charges Collected Since the Commission's Order. The Circuit Court of Appeals stayed the Commission's order pending appeal. The companies state that as a condition of the stay the court required them to give a bond in the sum of $1,000,000 conditioned upon their refund of excess charges to customers, in the event that the Commission's order should be sustained. The bond is not in the record and its precise terms are not before us.

The companies point out that substantially all the gas affected by the reduction in revenues is sold to wholesalers who distribute it for ultimate consumption. They argue that the purpose of the rate regulation is the protection of consumers, and that the purposes of the Act will not be effectuated by the refunds to wholesalers. They insist that such refunds, being the wholesalers' profits from past business, cannot be resorted to for reducing future rates to the consumers. *Cf. Knoxville* v. *Knoxville Water Co.*, 212 U. S. 1, 14; *Galveston Electric Co. v. Galveston, supra*, 395.

Of this contention it is enough to say that the question of the disposition of the excess charges is not before us for determination on the present record. Cf. *Morgan* v. *United States*, 304 U. S. 1, 26. Amounts collected in excess of the Commission's order are declared to be unlawful by § 4(a) of the Act. If there is any basis, either in the bond or the circumstances relied upon by the companies, for not compelling the companies to surrender these illegal exactions, it does not appear from the record.

We have considered but find it unnecessary to discuss other objections of lesser moment to the Commission's order. We sustain the validity of the order and reverse the judgment below.

Reversed.

Mr. Justice BLACK, Mr. Justice DOUGLAS, and Mr. Justice MURPHY, concurring.

I.

We concur with the Court's judgment that the rate order of the Federal Power Commission, issued after a fair hearing upon findings of fact supported by substantial evidence, should have been sustained by the court below. But insofar as the Court assumes that, regardless of the terms of the statute, the due process clause of the Fifth Amendment grants it power to invalidate an order as unconstitutional because it finds the charges to be unreasonable, we are unable to join in the opinion just announced.

Rate making is a species of price fixing. In a recent series of cases, this Court has held that legislative price fixing is not prohibited by the due process clause.[1] We believe that in so holding, it has returned in part at least to the constitutional principles which prevailed for the first hundred years of our history. *Munn* v. *Illinois*, 94 U. S. 113; *Peik* v. *Chicago, etc. Railway Co.*, 94 U. S. 164. Cf. *McCart* v. *Indianapolis Water Co.*, 302 U. S. 419, 427-428.

[1] Some of these cases arose under the Fifth, some under the Fourteenth Amendment. Nebbia v. New York, 291 U. S. 502 [state statute authorizing a milk control board to fix minimum and maximum retail prices for milk]; Mulford v. Smith, 307 U. S. 38 [federal statute imposing penalties on tobacco auction warehousemen for marketing tobacco in excess of prescribed quota]; United States v. Rock Royal Co-op., 307 U. S. 533 [federal statute authorizing Secretary of Agriculture to fix minimum prices to be paid producers for milk sold to dealers]; Sunshine Coal Co. v. Adkins, 310 U. S. 381 [federal statute

The *Munn* and *Peik* cases, decided in 1877, Justices Field and Strong dissenting, emphatically declared price fixing to be a constitutional prerogative of the legislative branch, not subject to judicial review or revision.

In 1886, four of the Justices who had voted with him in the *Munn* and *Peik* cases no longer being on the Court, Chief Justice Waite expressed views in an opinion of the Court which indicated a yielding in part to the doctrines previously set forth in Mr. Justice Field's dissenting opinions, although the decision, upholding a state regulatory statute, did not require him to reach this issue. See *Railroad Commission Cases*, 116 U. S. 307, 331. For an interesting discussion of the evolution of this change of position, see Swisher, Stephen J. Field, 372-392. By 1890, six Justices of the 1877 Court, including Chief Justice Waite, had been replaced by others. The new Court then clearly repudiated the opinion expressed for the Court by Chief Justice Waite in the *Munn* and *Peik* cases, in a holding which accorded with the views of Mr. Justice Field. *Chicago, &c. Railway Co.* v. *Minnesota*, 134 U. S. 418. Under those views, first embodied in a holding of this Court in 1890, "due process" means no less than "reasonableness judicially determined".[2] In accordance with this elastic meaning which, in the words of Mr. Justice Holmes, makes the sky the limit[3] of judicial power to declare legislative acts unconstitutional, the conclusions of judges, substituted for those of legislatures, become a broad and varying standard of constitutionality.[4] We shall not attempt now to set out at length the reasons for our belief that acceptance of such a meaning is historically unjustified and that it transfers to courts powers which, under the Constitution, belong to the legislative branch of government. But we feel that

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authorizing Bituminous Coal Commission to fix maximum and minimum prices for bituminous coal]; United States v. Darby, 312 U. S. 100 [federal statute fixing minimum wages (and maximum hours) for employees engaged in production of goods for interstate commerce]; Olsen v. Nebraska, 313 U. S. 236 [state statute fixing maximum compensation to be collected by private employment agencies].

[2] See Polk Company v. Glover, 305 U. S. 5, 12-19. Cf. Chambers v. Florida, 309 U. S. 227, 235-238.

[3] "As the decisions now stand, I see hardly any limit but the sky to the invalidating of those rights if they happen to strike a majority of this Court as for any reason undesirable." Baldwin v. Missouri, 281 U. S. 586, 595.

[4] To hold that the Fourteenth Amendment was intended to and did provide protection from state invasions of the right of free speech and other clearly defined protections contained in the Bill of Rights, Drivers Union v. Meadowmoor Co., 312 U. S. 287, 301-302, is quite different from holding that "due

we must record our disagreement from an opinion which, although upholding the action of the Commission on these particular facts, nevertheless gives renewed vitality to a "constitutional" doctrine which we are convinced has no support in the Constitution.

The doctrine which makes of "due process" an unlimited grant to courts to approve or reject policies selected by legislatures in accordance with the judges' notion of reasonableness had its origin in connection with legislative attempts to fix the prices charged by public utilities. And in no field has it had more paralyzing effects.[5]

II.

We have here, to be sure, a statute which expressly provides for judicial review. Congress has provided in § 5 of the Natural Gas Act that the rates fixed by the Commission shall be "just and reasonable". The provision for judicial review states that the "finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive." § 19(b). But we are not satisfied that the opinion of the Court properly delimits the scope of that review under this Act. Furthermore, since this case starts a new chapter in the regulation of utility rates, we think it important to indicate more explicitly than has been done the freedom which the Commission has both under the Constitution and under this new statute. While the opinion of the Court erases much which has been written in rate cases during the last half century, we think this is an appropriate occasion to lay the ghost of *Smyth* v. *Ames*, 169 U. S. 466, which has haunted utility regulation since 1898. That is especially desirable lest the reference by the majority to "constitutional requirements" and to "the limits of due process" be deemed to perpetuate the fallacious "fair value" theory of rate making in the limited judicial review provided by the Act.

Smyth v. *Ames* held (pp. 546-547) that "the basis of all calculations as to the reasonableness of rates to be charged by a corporation maintaining a highway under legislative sanction

process", an historical expression relating to procedure, Chambers v. Florida, *supra*, confers a broad judicial power to invalidate all legislation which seems "unreasonable" to courts. In the one instance, courts proceeding within clearly marked constitutional boundaries seek to execute policies written into the Constitution; in the other they roam at will in the limitless area of their own beliefs as to reasonableness and actually select policies, a responsibility which the Constitution entrusts to the legislative representatives of the people.

[5] McCart v. Indianapolis Water Co., *supra*.

must be the fair value of the property being used by it for the convenience of the public. And in order to ascertain that value, the original cost of construction, the amount expended in permanent improvements, the amount and market value of its bonds and stock, the present as compared with the original cost of construction, the probable earning capacity of the property under particular rates prescribed by statute, and the sum required to meet operating expenses, are all matters for consideration, and are to be given such weight as may be just and right in each case. We do not say that there may not be other matters to be regarded in estimating the value of the property. What the company is entitled to ask is a fair return upon the value of that which it employs for the public convenience. On the other hand, what the public is entitled to demand is that no more be exacted from it for the use of a public highway than the services rendered by it are reasonably worth."

(1) This theory derives from principles of eminent domain. See Mr. Justice Brewer, *Ames* v. *Union Pacific Ry. Co.*, 64 Fed. 165, 177; *West* v. *Chesapeake & Potomac Telephone Co.*, 295 U. S. 662, 671; Hale, Conflicting Judicial Criteria of Utility Rates, 38 Col. L. Rev. 959. In condemnation cases the "value of property, generally speaking, is determined by its productiveness—the profits which its use brings to the owner." *Monongahela Navigation Co.* v. *United States*, 148 U. S. 312, 328, 329. Cf. *Consolidated Rock Products Co.* v. *Du Bois*, 312 U. S. 510, 525-526. But those principles have no place in rate regulation. In the first place, the value of a going concern in fact depends on earnings under whatever rates may be anticipated. The present fair value rule creates but offers no solution to the dilemma that value depends upon the rates fixed and the rates upon value. See Mr. Justice Brandeis, *Southwestern Bell Telephone Co.* v. *Public Service Commission*, 262 U. S. 276, 292; Hale, The Fair Value Merry-Go-Round, 33 Ill. L. Rev. 517; 2 Bonbright, Valuation of Property, pp. 1094 *et seq.* In the second place, when property is taken under the power of eminent domain the owner is "entitled to the full money equivalent of the property taken, and thereby to be put in as good position pecuniarily as it would have occupied if its property had not been taken." *United States* v. *New River Collieries Co.*, 262 U. S. 341, 343. But in rate-making the owner does not have any such protection. We know without attempting any valuation that if earnings are reduced the value

will be less. But that does not stay the hand of the legislature or its administrative agency in making rate reductions. As we have said, rate-making is one species of price-fixing. Price-fixing, like other forms of social legislation, may well diminish the value of the property which is regulated. But that is no obstacle to its validity. As stated by Mr. Justice Holmes in *Block* v. *Hirsh*, 256 U. S. 135, 155: "The fact that tangible property is also visible tends to give a rigidity to our conception of our rights in it that we do not attach to others less concretely clothed. But the notion that the former are exempt from the legislative modification required from time to time in civilized life is contradicted not only by the doctrine of eminent domain, under which what is taken is paid for, but by that of the police power in its proper sense, under which property rights may be cut down, and to that extent taken, without pay." Somewhat the same view was expressed in *Nebbia* v. *New York*, 291 U. S. 502, 532, where this Court said: "The due process clause makes no mention of sales or of prices any more than it speaks of business or contracts or buildings or other incidents of property. The thought seems nevertheless to have persisted that there is something peculiarly sacrosanct about the price one may charge for what he makes or sells, and that, however able to regulate other elements of manufacture or trade, with incidental effect upon price, the state is incapable of directly controlling the price itself. This view was negatived many years ago. *Munn* v. *Illinois*, 94 U. S. 113." Explicit recognition of these principles will place the problems of rate-making in their proper setting under this statute.

(2) The rule of *Smyth* v. *Ames*, as construed and applied, directs the rate-making body in forming its judgment as to "fair value" to take into consideration various elements—capitalization, book cost, actual cost, prudent investment, reproduction cost. See Mr. Justice Brandeis, *Southwestern Bell Telephone Co.* v. *Public Service Commission*, *supra*, pp. 294-295. But as stated by Mr. Justice Brandeis: "Obviously 'value' cannot be a composite of all these elements. Nor can it be arrived at on all these bases. They are very different; and must, when applied in a particular case, lead to widely different results. The rule of *Smyth* v. *Ames*, as interpreted and applied, means merely that all must be considered. What, if any, weight shall be given to any one, must practically rest in the judicial discretion of the tribunal which

makes the determination. Whether a desired result is reached may depend upon how any one of many elements is treated." *Id.*, pp. 295-296. The risks of not giving weight to reproduction cost have been great. *Southwestern Bell Telephone Co.* v. *Public Service Commission, supra; St. Louis & O'Fallon Ry. Co.* v. *United States,* 279 U. S. 461. The havoc raised by insistence on reproduction cost is now a matter of historical record. Mr. Justice Brandeis in the *Southwestern Bell Telephone* case demonstrated how the rule of *Smyth* v. *Ames* has seriously impaired the power of rate-regulation and how the "fair value" rule has proved to be unworkable by reason of the time required to make the valuations, the heavy expense involved, and the unreliability of the results obtained.[6] And see Mr. Justice Brandeis concurring, *St. Joseph Stock Yards Co.* v. *United States,* 298 U. S. 38, 73; dissenting opinion, *McCart* v. *Indianapolis Water Co.,* 302 U. S. 419, 423 *et seq.*; Mr. Justice Stone dissenting, *West* v. *Chesapeake & Potomac Telephone Co., supra.* The result of this Court's rulings in rate cases since *Smyth* v. *Ames* has recently been summarized as follows: "Under the influence of these precedents, commission regulation has become so cumbersome and so ineffective that it may be said, with only slight exaggeration, to have broken down. Even the investor,[7] on whose behalf the constitutional safeguards have been developed; has received no protection against the rebounds from the inflated stock-market prices that are stimulated by the 'fair-value' doctrine." Bonbright, *op cit.*, p. 1154.

As we read the opinion of the Court, the Commission is now freed from the compulsion of admitting evidence on reproduction

[6] "The relation between the public utility and the community cannot be expressed in terms of a simple, quantitatively ascertainable fact, for the relation involves numerous and complex factors which depend on compromise and practical adjustment rather than on deductive logic. The whole doctrine of *Smyth* v. *Ames* rests upon a gigantic illusion. The fact which for twenty years the court has been vainly trying to find does not exist. 'Fair value' must be shelved among the great juristic myths of history, with the Law of Nature and the Social Contract. As a practical concept, from which practical conclusions can be drawn, it is valueless." Henderson, Railway Valuation and the Courts, 33 Harv. L. Rev. 1031, 1051.

[7] "Such valuation proceedings, as heretofore conducted, are excessively costly, require a long period of time, affect adversely the corporation's credit, interfere with its financing upon favorable terms, and frequently cause the postponement of extensions and improvements to the great detriment of the public. Unless and until there is some change in the legal principles which must be applied in determining fair value, however, the industry cannot escape from this situation." Report of the Committee on Valuation, American Electric Railway Assoc., 1924, p. 20.

cost or of giving any weight to that element of "fair value". The Commission may now adopt, if it chooses, prudent investment as a rate base—the base long advocated by Mr. Justice Brandeis. And for the reasons stated by Mr. Justice Brandeis in the *Southwestern Bell Telephone* case there could be no constitutional objection if the Commission adhered to that formula and rejected all others.

Yet it is important to note, as we have indicated, that Congress has merely provided in § 5 of the Natural Gas Act that the rates fixed by the Commission shall be "just and reasonable". It has provided no standard beyond that. Congress, to be sure, has provided for judicial review. But § 19(b) states that the "finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive." In view of these provisions we do not think it is permissible for the courts to concern themselves with any issues as to the economic merits of a rate base. The Commission has a broad area of discretion for selection of an appropriate rate base. The requirements of "just and reasonable" embrace among other factors two phases of the public interest: (1) the investor interest; (2) the consumer interest. The investor interest is adequately served if the utility is allowed the opportunity to earn the cost of the service. That cost has been defined by Mr. Justice Brandeis as follows: "Cost includes not only operating expenses, but also capital charges. Capital charges cover the allowance, by way of interest, for the use of the capital, whatever the nature of the security issued therefor; the allowance for risk incurred; and enough more to attract capital." *Southwestern Bell Telephone Co.* v. *Public Service Commission, supra,* p. 291. Irrespective of what the return may be on "fair value", if the rate permits the company to operate successfully and to attract capital all questions as to "just and reasonable" are at an end so far as the investor interest is concerned. Various routes to that end may be worked out by the expert administrators charged with the duty of regulation. It is not the function of the courts to prescribe what formula should be used. The fact that one may be fair to investors does not mean that another would be unfair. The decision in each case must turn on considerations of justness and fairness which cannot be cast into a legalistic formula. The rate of return to be allowed in any given case calls for a highly expert judgment. That judg-

ment has been entrusted to the Commission. There it should rest.

One *caveat* however should be entered. The consumer interest cannot be disregarded in determining what is a "just and reasonable" rate. Conceivably a return to the company of the cost of the service might not be "just and reasonable" to the public. The correct principle was announced by this Court in *Covington and Lexington Turnpike Co.* v. *Sandford*, 164 U. S. 578, 596:

"It cannot be said that a corporation is entitled, as of right, and without reference to the interests of the public, to realize a given per cent upon its capital stock. When the question arises whether the legislature has exceeded its constitutional power in prescribing rates to be charged by a corporation controlling a public highway, stockholders are not the only persons whose rights or interest are to be considered. The rights of the public are not to be ignored. It is alleged here that the rates prescribed are unreasonable and unjust to the company and its stockholders. But that involves an inquiry as to what is reasonable and just for the public. If the establishing of new lines of transportation should cause a diminution in the number of those who need to use a turnpike road, and, consequently, a diminution in the tolls collected, that is not, in itself, a sufficient reason why the corporation, operating the road, should be allowed to maintain rates that would be unjust to those who must or do use its property. The public cannot properly be subjected to unreasonable rates in order simply that stockholders may earn dividends." Cf. *Chicago & Grand Trunk Ry. Co.* v. *Wellman*, 143 U. S. 339, 345-346; *United Gas Co.* v. *Texas*, 303 U. S. 123, 150-151.

This problem carries into a field not necessary to develop here. It reemphasizes however that the investor interest is not the sole interest for protection. The investor and consumer interests may so collide as to warrant the rate-making body in concluding that a return on historical cost or prudent investment though fair to investors would be grossly unfair to the consumers. The possibility of that collision reinforces the view that the problem of rate-making is for the administrative experts not the courts and that the *ex post facto* function previously performed by the courts should be reduced to the barest minimum which is consistent with the statutory mandate for judicial review. That review should be as confined and restricted as the review, under similar statutes, of orders of other administrative agencies.

Mr. Justice FRANKFURTER, concurring.

I wholly agree with the opinion of the CHIEF JUSTICE.

Congress has in the Natural Gas Act specifically cast upon courts the duty to review orders of the Federal Power Commission fixing "just and reasonable" rates. The constitutional scope of judicial review of rate orders where Congress has denied judicial review is therefore not in issue in this case. Discussion of the problem is academic, especially since we all concur in the CHIEF JUSTICE's conclusions on the rate order here made by the Commission. But since the issue has been stirred, I add a few words because legal history still has its claims.

While the doctrine of "confiscation", as a limitation to be enforced by the judiciary upon the legislative power to fix utility rates, was first applied in *Chicago &c. Railway Co.* v. *Minnesota*, 134 U. S. 418, that decision followed principles expounded in *Stone* v. *Farmers' Loan & Trust Co.*, 116 U. S. 307, especially at 331. See 134 U. S. at 455-56. Mr. Chief Justice Waite, who delivered the opinion in the *Stone* case as well as in the earlier decision in *Munn* v. *Illinois*, 94 U. S. 113, was therefore the author of the doctrine of "confiscation" and its corollary, "judicial review". His view was shared by such stout respecters of legislative power over utilities as Mr. Justice Miller (see Fairman, Mr. Justice Miller and the Supreme Court, *passim*), Mr. Justice Bradley (see his dissent in *Chicago &c. Railway Co.* v. *Minnesota*, 134 U. S. 418, 461), and Mr. Justice Harlan. The latter, indeed, agreed with Mr. Justice Field that the regulatory power exercised in the *Railroad Commission Cases*, 116 U. S. 307, constituted an impairment of the obligation of contract. By no one was the doctrine of judicial review more emphatically accepted, and applied in favor of a public utility, than by Mr. Justice Harlan in the decision and opinion in *Covington &c. Turnpike Co.* v. *Sandford*, 164 U. S. 578, especially at 591-95.

But while this historic controversy over the constitutional limitations upon the power of courts in rate cases is not presented here, if it be deemed that courts have nothing to do with rate-making because that task was committed exclusively to the Commission, surely it is a usurpation of the Commission's function to tell it how it should discharge this task and how it should protect the various interests that are deemed to be in its and not in our keeping.